VOLUME 11 FEBRUARY 1949 NUMBER

COLLEGE OF COMMERCE AND BUSINESS ADMINISTRATION

CURRENT ECONOMIC COMMENT

Formerly Opinion and Comment

UNIVERSITY OF ILLINOIS BULLETIN

CURRENT ECONOMIC COMMENT

Formerly *Opinion and Comment*

Published quarterly by Bureau of Economic and Business Research
College of Commerce, University of Illinois

This quarterly publication of the Bureau of Economic and Business Research presents factual information and interpretive comment on economic developments, business operations, public policy, and related questions of current interest. It is available on request.

The opinions expressed in the articles are the personal views of the respective authors and not necessarily those of the College of Commerce or the University.

Address communications to Bureau of Economic and Business Research, 205 David Kinley Hall, Urbana, Ill.

UNIVERSITY OF ILLINOIS BULLETIN

Volume 46; Number 56; March, 1949. Published seven times each month by the University of Illinois. Entered as second-class matter December 11, 1912, at the post office at Urbana, Illinois, under the Act of August 24, 1912. Office of Publication, 358 Administration Building, Urbana, Illinois.

The Cold War: Ideological Conflict*

Howard R. Bowen

Dean, College of Commerce and Business Administration, University of Illinois

We can all agree that foreign relations are overwhelmingly significant in determining the future of the United States. The conduct and outcome of our foreign relations are likely to decide not only the course of business activity and prices, but also the ultimate survival of our political and economic institutions, and even the survival of the human race itself.

The fundamental condition of our present foreign relations is the almost unbearable tension between Russia and the United States. Will this tension end in full-scale war? If so, how soon? If not, will there be a long period of armed truce or cold war? These are the questions for which we must seek answers if we are to try to foresee what may lie ahead for American business.

When we ask: Is the inflation likely to continue? or, Is a recession in business activity imminent? or, Is business likely to be subjected to additional governmental controls?, the replies depend, I think, on our answer to the more basic question: Is war with Russia likely, and if so, when?

Obviously, no one knows the answer to this question, and there is no certain way of finding out. The correct approach to the question, however, is to turn back the pages of history in order to examine what has caused earlier wars, and to see whether the kind of causation which has applied in the past is applicable to the present state of tension between Russia and the United States.

Historical Causes of War

Looking back over history, there have been eight principal causes of wars. Not all of these causes have been operative in every war, and there have been few wars where only one of them has been operative. But these eight causes, in varying combinations, have been at the root of most wars.

Territory. First, the earliest and perhaps most frequent cause of war has been the desire of a tribe or nation or state to increase the amount of its territory and natural resources. In many cases, this desire has arisen as a result of overpopulation. In most societies the growth of population has been so rapid as to cause eventually a scarcity of food and other means of livelihood. This scarcity could be overcome in three ways: (1) by limiting the birth rate and thus reducing the population; (2) by improving the technology; or (3) by expanding the territory occupied by the group. Most peoples have been unable or unwilling to limit the birth rate; they have been unable to improve their technology for want of scientific knowledge and capital; and so they have been tempted to go to war to expropriate the territory of their neighbors. The potential victims of such aggression, on the other hand,

*Address before the Illinois Bankers Conference, Urbana, November 18, 1948.

have been tempted to warlike activity in order to defend their position. The victors in such wars have often driven out or exterminated the vanquished in order that they might exploit the territory exclusively. The Bible is full of the stories of such wars, and many wars between primitive tribes have been concerned principally with territory.

Sometimes, however, the desire of a tribe or nation to expand its territory originated not in the pressures of overpopulation but simply in the desire to increase the wealth of the group at the expense of other groups. In primitive times, especially, there was always a tendency to forage on the territory of neighboring tribes. Among more advanced peoples, a special temptation always existed to take over territory from peoples having an inferior level of culture and technology. For example, if a rich territory were inhabited by primitive peoples who used it only for hunting and fishing or simple agriculture, people of advanced culture were tempted to take over because they could make better use of the territory than its primitive occupants. Much of Africa and Asia and all of the Americas, including the United States, were conquered and settled on this principle. European peoples of advanced culture merely took over from primitive Negroes, Mongolians, Aztecs, or Indians — always with numerous wars and skirmishes. The Italian conquests in Africa prior to World War II were of this nature also. The Italians proposed simply to take over and colonize territory which had previously been occupied by Ethiopians and other people of less advanced culture and technology.

In the present conflict, the desire for territory is not a prime cause. Russia and the United States are both conspicuous as countries of vast area and of magnificent natural resources. Neither exhibits any particular interest in land merely for the sake of land — though, of course, both are concerned about land for strategic reasons.

Plunder. A second frequent cause of wars has been the desire to obtain plunder, tribute, taxes, reparations, or slaves. This was an element in most tribal wars; the Roman conquests may have been motivated in part in this way; and in many other wars, the desire for booty may have been a factor.

Although the Russians have exhibited a somewhat avid interest in reparations and undoubtedly plundered conquered territory during the recent war, yet it is utterly fantastic to believe that they would seriously consider starting a war for the plunder they might get. The costs of the war would so obviously exceed the value of any imaginable booty as to rule out this cause entirely. And surely no one — not even the Russians — supposes that the United States is interested in booty.

Raw Materials and Markets. A third cause of war has been the desire of industrial countries to obtain assured sources of raw materials and assured markets. This was an important factor in most of the warfare involving the western European countries from the 15th century to modern times. This also explains in part the more recent warlike behavior of Japan, Germany, and Italy.

The concern of rising industrial nations for raw materials and markets

was due to the fact that each was dependent for its livelihood upon foreign sources of food and raw materials, and each was dependent upon foreign markets to provide the wherewithal to buy these raw materials. Each was tempted to secure or improve its position, and thus to insure its future prosperity, by controlling its sources of livelihood. Thus each was tempted to undertake colonial adventures. The result, of course, was a series of colonial wars in all parts of the world. But the success of one industrial country in this game was a threat to another. Hence, the process led also to wars among the competing industrial countries. In the rivalry lasting over several centuries, England emerged dominant. This largely explains the unique position of England, especially during the 19th century.

Today, neither Russia nor the United States is the kind of country that would be expected to go to war for raw materials or markets. Both countries are outstanding examples of virtual self-sufficiency. Their industrial establishments are largely oriented toward domestic raw materials and domestic markets. It is true that each is dependent upon outside sources for certain minor but strategic materials and that each could profit from a considerable foreign trade. But the fact remains that Russia and the United States are the most conspicuous cases of countries that do not depend upon the outside world and have no serious balance-of-payment problem. It is quite unimaginable that either would go to war or threaten war to get foreign sources of raw materials and foreign markets. A possible exception to this statement is that each is concerned over the control of certain strategic materials — notably oil and the heavy atomic elements — yet I think one can say that this concern is more largely a *result* rather than a primary cause of the conflict.

Investment. Fourth, the desire to secure outlets for capital investment and to protect existing capital investments has led to war. Advanced industrial countries have invariably amassed considerable supplies of capital. As more and more domestic investments in plant, equipment, and public works have been made, the actual and prospective rate of return on capital has declined. (One of the most dependable laws of economics is that as a country increases its domestic capital, the rate of return on capital, that is, the interest rate, declines.) Eventually, in the more mature and wealthy countries a point has been reached at which foreign investment has become more attractive than domestic. In some cases, the near-saturation of domestic opportunities for investment made the search for foreign outlets essential to the continuation of prosperity and full employment. Such countries became exporters of capital which made them owners of foreign factories, public utility plants, railroads, and plantations, and which made of them creditors of foreign governments and foreign citizens and companies. Influential classes in such capital-exporting countries often swayed governmental policy toward creating the kind of conditions abroad which would open up opportunities for reasonably secure foreign investment and which would

protect such investments once they had been made. This led the governments of such countries to intervene in the affairs of the less well-developed countries which offered the more attractive markets for capital. The intervention varied from making treaties and establishing "spheres of influence" to actually reducing the backward territories to colonial status or to sending in the marines and taking over the public revenues.

This entire process led to wars between advanced industrial countries and backward nations, and also between industrial countries which found themselves in competition with one another for the exclusive privilege of exporting capital to particular backward areas. The relations between industrial countries like England, Holland, and the United States and less advanced territories like India, the Middle East, Indonesia, China, and parts of Latin America can be explained in part by the desire of the industrial countries to develop and hold outlets for capital investment. Similarly, the effort of the Austro-Hungarian Empire to unify the Balkans is a case in point. Also, the recent warlike behavior of Germany and Japan can be explained in part by the fact that each of these countries rose to industrial eminence later than some of its rivals. By the time they were ready to export capital, the most productive outlets for investment had been preempted by England, France, and the United States. The latecomers attempted to overcome their disadvantage by conquering their more fortunate rivals.

The desire to secure outlets for capital and to protect existing investments must also be ruled out as a cause of present tension. Russia has virtually no foreign investments and is not interested in making any. Russia is desperately short of capital and has been engaged ever since the Revolution in building up its internal capital equipment — even to the extent of reducing its people to a state of near-starvation. Such a country is not looking for places to put its capital abroad. The United States, on the other hand, has at various times been a heavy capital exporter and at present has substantial foreign holdings. Moreover, we (or at least our capitalists) could probably benefit in the long run if our outlets for foreign investment were expanded — for example, if areas like the Far East were stabilized politically so that secure investments could be made. However, it seems to me fantastic that the United States would undertake aggression — especially risk a war with Russia — for the sake of its capital investments.

Transportation Routes. Fifth, the desire to acquire and hold strategic transportation routes or facilities has frequently led to conflict. This cause of wars is, of course, related to the desire to get reliable sources of raw materials, dependable markets, and safe foreign investments. For example, in order for Britain to maintain her interests in the Middle East, Africa, India, Australia, and China, the Mediterranean and the Suez Canal became vital and sensitive nerve centers of Empire policy. Similarly, the Isthmus of Panama became important to us.

The perennial quest of Russia for

warm water ports and for control of the Dardanelles comes under this heading. However, it is doubtful whether Russian dissatisfaction in this quarter would be a major cause of war. Because of her relative self-sufficiency, Russian interests are not primarily in foreign trade. They are, first and foremost, directed toward internal economic development. There is no strategic transportation route that concerns Russia in the same way that the "lifeline of the Empire" concerns Britain. Moreover, Russia's traditional problem in the Baltic has largely been solved as a result of the recent war, which gave her Latvia, Esthonia, Lithuania, part of Finland, part of Poland, and possibly part of Germany. However, the problem of the Dardanelles and of access to the Mediterranean is still a live issue and surely represents one of Russia's objectives. Indeed, the whole Middle-Eastern problem, as it is influenced by the interests of the great powers, is affected by Russia's desire to break out to the south.

Religion. Sixth, the attempt to propagate a particular religious faith, to stop the spread of an alien religious faith, or to gain possession of a holy city or a sacred relic have fomented many wars. Frequently, religious motives have been mixed with more mundane considerations; yet it cannot be denied that religion has on occasion been an important and independent factor in the causation of wars. Examples are the Crusades of the Middle Ages and the Thirty Years' War of the 17th century.

In the present conflict between Russia and the United States, religion — at least in the conventional sense — is not a major consideration.

Power. Seventh, the desire for power and prestige on the part of a nation or its leaders. This cause of wars has appeared in various forms, for example: the attempt of a princely dynasty or a nationalistic state to extend its power and domain; the ambition of a persuasive leader like Napoleon or Hitler; the desire of a gifted ruling class like the British aristocracy to obtain outlets and opportunities for its talents in public administration; or the desire to go to war for the sake of adventure or psychological release. All these forms are alike in that the motivation is power for its own sake. Most frequently, I think, these causes of war appear in combination with other causes. Nevertheless, they are almost always present as accentuating, complicating, or conditioning factors.

It is easy to interpret the Russian leadership today as a group of power-hungry madmen who are out to conquer the world merely for the sake of the power they would get. I realize that there can be differing opinions on this point and I surely would not deny that lust for power may figure as a cause of present tension. Yet, my interpretation of the Russian leadership is that they have all they can handle at home and are concerned primarily with making a go of state socialism at home. They are confronted with almost insuperable problems in their own back yard which must be solved before it makes any sense for them to be thinking about world domination *for its own sake.* I do not mean by this that they

are not interested in world domination; I mean only that they are not interested in it *for its own sake.* The whole significance of the struggle between Stalin and Trotzky — a struggle that was won by Stalin — was that Russia must consolidate its own position before embarking upon foreign adventures. Even the orthodox Marxist line that Communism must one day sweep the world is not based on the desire of a ruling clique for world power. Rather, it is based upon the belief that Communism in any one territory would never be safe from foreign aggression until Communism was established everywhere.

Revolution. Finally, dissatisfaction over important domestic issues has been the cause of civil wars. Through the ages, dissident elements have attempted to overthrow established governments, or established governments have attempted to subdue rebellious groups. The result has been a long series of bloody conflicts from which few countries have been immune. The present state of tension can hardly be described as a domestic revolution leading toward civil war.

Real Cause of the Present Cold War

I have listed what I consider the main causes of past wars, and I have indicated that, in my judgment at least, these causes — singly or in combination — are not sufficient to explain the present state of tension between Russia and the United States. Does this mean that the present conflict is superficial and unlikely to lead to war? Not at all. Rather, it means that the historic causes of war do not fit this situation, and that to understand the causes of the present conflict, and thus to assess the probability of war, we must search for a new cause or causes that may not have operated prominently in the past. In my judgment, the dominating cause today is *difference in ideologies,* that is, *difference in the political and economic ideas and practices of Communism and Capitalism.*

That the fundamental force which divides Russia and the United States is in the realm of ideas rather than in the realm of tangible economic interests does not mean that the conflict is unimportant or unlikely to break out in war. Religious wars were fought over ideas, too, and wars of religion have been notable for their fierceness and for the implacable enmity of the rivals.

The world today is divided into two kinds of opposing social systems: Communist and Capitalist. Russia represents the center and focus of power of the Communist world, and the United States represents the center and focus of power of the Capitalist world. Surrounding these two major powers are other countries espousing social systems at various stages intermediate between Communism and Capitalism. These other countries are oriented more or less definitely either toward Russia or toward the United States.

Communist Insecurity. The Russian world is engaged in a vast experiment to determine whether a people can live successfully and happily in a society organized along Communist lines. The Communist system is, however, on the defensive. It has not achieved the golden age promised by its leaders. It has brought bureaucratic red tape,

hardship, starvation, and suppression. It has not produced the high standard of living, the equality in income, and the flowering of human rights that had been promised by the Revolutionary leaders. True, many of the difficulties of Communism are attributable to the war and the necessity to prepare for war. Yet, even with due allowance for the effects of war, it has been demonstrated neither within Russia nor abroad that Communism is the answer to the political and social needs of the 20th Century. Communist leadership knows this and is basically apprehensive about its position and about the future of the social system to which it is committed. This apprehension is reinforced by the teachings of orthodox Marxist doctrine, which holds that Communism cannot survive in a capitalist world and that the security of Communism can be assured only if it becomes world-wide. This doctrine is reinforced in the minds of Russians by the fact that Communist Russia has been attacked by Western powers twice in one generation: first, during and following the Russian Revolution, and second, during the recent World War when Russia was invaded by Germans who declared that it was their sacred mission to stamp out Communism. Russian suspicions were also kindled by her experiences in the League of Nations where Russia was "let down" by the Western powers when her representative, Litvinov, attempted to invoke the principle of collective security against aggressors. As a result of all these influences, we have today a suspicious, apprehensive, and desperate nation whose leadership is seriously worried about the future and which is preoccupied with strengthening its power and its strategic position. In this situation, also, it is strongly tempted to divert the attention of its citizens from internal difficulties and disappointments by directing their attention to foreign enemies.

Capitalist Insecurity. On the other hand, the capitalist world, of which the United States is the center, is also engaged in an equally great experiment to determine whether a system of private enterprise and free political institutions can survive and prosper in the modern world. This system is also on the defensive. The United States, in a sense, represents the last capitalist outpost in the world. Almost all other important countries even outside the Russian sphere have moved to the left a considerable distance. Even within the United States, capitalist institutions are under attack. There are many problems, especially those relating to inequality, insecurity, and unemployment that have not been solved within our capitalist system. It is true that these problems are temporarily in abeyance during our present extended period of prosperity. But we all know realistically that this prosperity probably cannot last forever and that, if and when it comes to an end, there will be stirrings in the populace and strong political pressure for increasing governmental controls over our economic life. This explains, I think, why American leadership today is fundamentally insecure. This insecurity itself explains why there is so much conscious effort to "sell" capitalist institutions and to "educate" the public on the virtues of

free enterprise, even at a time when there is little popular pressure for revision of our basic institutions.

Intolerability of Difference. The situation in the modern world then, is about like this: there are two great nations with fundamentally different ideologies and social institutions; and the leadership in each nation is plagued with profound feelings of insecurity and apprehension regarding the stability and survival-value of its kind of system.

Under these conditions, the success of either of the two great nations in operating its kind of social system is a threat to the other. For example, the achievement of a high standard of living and of economic stability within Russia would be an enormous blow to capitalism in the United States. Such an accomplishment would give great appeal to left-wing political movements in this country and would endanger the very foundation of American private enterprise. On the other hand, the success of capitalism is equally repugnant to the Russian leadership. If it could be shown unequivocally that the United States could operate a system of free enterprise with stability, high standards of living, reasonable security, and social justice, all the props would go out from beneath the Communist ideology. Russia would then have nothing to sell its people and no reason for asking them to undergo all the sacrifices she now demands. That is why the Communist leadership is so vocal in its predictions of an economic collapse in this country, so fervently wishes for the collapse to occur, and is so obviously disappointed as each month goes by without bringing the expected downfall. As a matter of fact, one of the leading Russian economists, Vargas, has been in disgrace because he has predicted a long period of prosperity in the United States, a prediction that is directly contrary to orthodox Marxist doctrine, which holds that capitalist countries are always inevitably subject to frequent and violent economic fluctuations.

My main conclusion, then, is that the present state of tension between Russia and the United States is due primarily to the fact that the two countries are trying to operate different kinds of social systems with different ideologies.

The point I am trying to make was recently expressed by an eminent psychiatrist. He said that when groups are insecure they cannot accept differences between them and other groups. The very existence of the difference is an admission that things could be another way. The difference is regarded as an insurmountable threat. Therefore, each group organizes itself tightly to resist the threat of the other group. Instead of accepting differences and living with them in a spirit of mutual give-and-take, they become aggressive in their reactions toward one another.

The nearest historic parallel to the present situation was in the relations between France and other European countries during and after the French Revolution. The effect of the overthrow of the French monarchy was electric throughout all countries having large remnants of feudalism. The very existence of a near-by country which had overthrown its monarchy was a

threat to established institutions throughout Europe. The ideological differences between the European aristocracy and the French democratic leaders were surely a significant factor leading to the Napoleonic wars.

Conclusions

Now what is the significance of the conclusion that the present state of tension is primarily ideological? First, it means that the danger of war is not therefore less than it would be if the conflict were over territories or colonies. Second, it means that the issue cannot be settled by giving Russia this territory, or that colony, or that trade concession, or any material thing. Settlement can come only through an accommodation based on the principle of live and let live, or arrived at through the evolution of both societies toward more compatible social structures and ideologies.

On the other hand, there is nothing but the unwillingness or inability of Russia and the United States to tolerate ideological differences that prevents good relations between the two. For example, there is inherently nothing that prevents a fruitful commerce, abundant cultural relations, free movement of peoples, and a general spirit of mutual respect and tolerance between Russia and ourselves. But it will not be easy to persuade the Russians with their ideological fixations, their iron curtains, and their overwhelming suspicion. It is an open question whether there can be any common meeting ground between social systems so diametrically opposed as Communism and Capitalism, or whether the peoples of the two ideologies can ever learn to understand and to trust one another. And so, if one is realistic, he must conclude that at best many long years will be required to reach an accommodation with Russia. We must look forward, I think, to many years of cold war, armed truce, unpleasant incidents, fear of war, rearmament, jockeying for position, aggressive propaganda, attempts to foment strife in capitalist countries, and all the unpleasant things we have experienced during the past several years. The differences are too fundamental, the issues too vital and too close to the interests of the leadership in both countries, to make possible an easy adjustment.

On the other hand, I do not believe that war is near or that it is wished by the leadership or the people in either Russia or the United States. In both countries the desire for peace and the need for peace are overwhelmingly great. Russia, in particular, is in the midst of a gigantic effort to rebuild and restore the country after the devastations of war. She needs a long period of peace in which to give the people some of the goods and the leisure and the security that have been promised by the Communist leadership.

It is reasonable to expect (or at least hope), therefore, that full-scale war may be postponed for several or even many years. In the interim, we can hope that the needed accommodation with our ideological opposites, the Russians, can be achieved and that the disaster of war may be averted altogether. One of the factors that makes one hopeful on this score is that the consequences of war with modern

weapons are obviously so terrible and the danger of total annihilation so great that leadership both here and abroad may become united in seeing the absolute necessity of avoiding war at all costs. My better judgment tells me, however, not to count on this.

But regardless of whether we shall eventually avoid war, we can be fairly sure that in the years immediately ahead, even though we may not be at war, neither will we be at peace. We shall not be able to disarm or to relax our vigilance.

As a recent editorial in the London *Economist* states: "The true course for the Western nations to pursue is to do everything that is necessary to make it clear to everybody that they both can and will defend the present boundaries of the free world, and to prove within those boundaries that their way of life is stronger, richer, and more appealing to men's minds than the doctrine and practices of Soviet Communism."

In this state of affairs, we must expect a continuation of large budgets for the armed forces and in support of our foreign policy. The resulting large expenditures of the Federal government — I would not venture to suggest how large they may become — will be a powerful force supporting the level of production, employment, and prices in this country. Although business fluctuations and recessions may lie ahead, they will probably be mitigated by the necessities of our foreign policy.

The Merchants' Merry-Go-Round

Robert D. Loken

Professor of Management, University of Illinois

FOR MORE THAN three years the merchants of the country have been verbally "girding their loins" for that fateful, on-rushing day when their lush and lenient "Seller's Market" would be replaced by the old rough and tough "Buyer's Market." Now that the long-heralded day has actually put in an appearance, at least in certain retail areas, the average merchant finds his staff woefully inadequate to cope with the "new" customer attitudes. Despite all the "planning" which was done to get ready for this very situation, few stores actually *did* anything to ease the strain and bruising which must result whenever people, primarily salespeople in this case, are forced into a new mold.

The only basic modifications required by the "new" market are changes in the habits and attitudes of those persons employed in buying merchandise for sale, or in actually selling that merchandise. Since, in most stores, management maintains close personal control of the buying function the problem narrows down to one of retraining the sales force. Some stores have made great strides in this undertaking; many stores have done little or nothing about it; but most stores have made sporadic, "shot-in-the-arm," and rather futile attempts to meet the problems.

To the average merchant the main threat in the Buyer's Market is the alarming increase in expense ratios. The typical solution to the problem of higher operating expenses is for the merchant to break into a dervish dance of expense control and cost reductions. For a period of days — or weeks — depending on the memory-span of the boss, the entire store from bottom to top suffers agonies of strangulation as each nickel and dime is squeezed of its very essence. Coincident with these "economy drives" there usually appears a strong (and expensive) sales promotion program to drive customers into the store. And so the employees find themselves caught between two fires — the expense axe on the one side and increasingly critical customers on the other. Under such pressures something has to give way. That "something," in this case, is the employees' morale. It appears to the rank-and-file employee that everything but the employee is included in the planning.

This is an illustration of the opportunistic attitude which most merchants have with regard to their personnel programs. It is the type of business shortsightedness which has governed retailing for a generation and has cost the average merchant thousands of profit dollars. This failure to operate under a planned personnel program is largely responsible for the excessive personnel turnover rate in stores during the past twelve months. This turnover rate was more than 50 per cent, whereas the rate for industry in the same period was only half as large.

While a drive to reduce expenses may show immediate savings, they are "expensive" savings from the long

view. Consider the reaction of the rank-and-file employee when top management decides that costs must be cut — that the frills must go. The net effect on the employee is always a heightening of insecurity. The old fears are aroused: "Maybe my job will be cut next." Everyone gets jittery and the oldtimers sigh and wearily remark: "Here we go again!"

It is a constant source of amazement that the same merchant who spends days or weeks planning a special promotion, or laying out seasonal buying plans, operates in the personnel field on an "off-the-cuff" basis, with almost no planning at all. Yet these same "unplanned for" employees are the people who can make or break the carefully master-minded sales plans.

Though there are many excellent reasons for planning a personnel program, perhaps the strongest is the appeal to the profit motive. At present there are approximately 15 million people employed in trade and service businesses over the country. With turnover at the present level of 50 per cent, this means that 7½ million of these employees changed jobs last year. Even if the cost of replacing each employee is figured at the bare minimum of $100 for costs of hiring, training, and lost sales, the merchants paid a tremendous price for the privilege of not planning their personnel operation last year. At $100 each for 7½ million replacements their bill was $750 million — three-quarters of a billion dollars thrown out the window! Even if they had cut this figure in half, as industry did, and kept turnover to a "reasonable" 2 per cent a month, the savings would have meant a tidy $375 million in the black.

It should be obvious that the task of raising the level of the sales force of a store to meet the more exacting demands of the Buyer's Market would be greatly simplified if the rate of employee turnover could be reduced through better personnel programs. Under present conditions the "average" salesperson stays on the job for only six months, which is hardly sufficient time to develop the seasoned, professional salespeople required by customers today. This becomes even more important when it is realized that this means that many salespeople don't last even two months on the job. One untrained salesperson can antagonize more customers than a good promotion can bring into the store.

Even more disastrous is the fact that turnover, like inflation, tends to be self-perpetuating. The fact that large numbers of people quit their jobs in turn influences coworkers to quit also, and a spiraling effect develops. Worst of all, this condition gradually becomes publicized and results in poor public relations, which in turn lower the level of applicants applying for work in a retail store. Stores have little prestige value for the labor force of the country. They occupy a low rung on the employment ladder, as evidenced by the expression heard regularly among those looking for jobs: "Oh well, if worst come to worst I can always get a job as a clerk in a store."

On the whole, retailers have done an excellent publicity job of selling their wares to their potential customers. They have done a poor job of selling the merits of stores and their importance in the community. A national survey was conducted last year by the

Opinion Research Corporation to find out what the public thought about some of our community services and institutions. The results of this survey underline the need for an organized program of public and personnel relations in stores. In answer to the question: "What is your town's most *important* business?", stores come out at the bottom of the list, below utilities, insurance companies, banks and financial institutions. In fact, "stores" were mentioned by only 10 per cent of the people polled. In answer to the question: "Which business pays the best *wages?", stores* again took *last* place. To the question: "Which business has the best *employee benefit* plan?", the answer put *stores* next to the *last.* To the question: "In which business is the public treated with the most *courtesy* and *friendliness?",* the public answer again put *stores* next to the bottom. Answers to other questions were equally disparaging for the stores but these few examples should make the point with sufficient strength. The public thinks that: (1) stores aren't important; (2) stores pay poor wages; (3) stores pay scant attention to employees; and (4) stores make little effort to be friendly and courteous.

In actual fact, none of these "public beliefs" are true. Stores play a very important and vital part in community life; they pay good wages; they invest a great deal of effort and money in employee benefits; and they maintain a high level of courtesy. Unfortunately, it doesn't matter what the facts are if the public doesn't believe in their truth. In a nutshell — stores have not "sold" themselves, their services, or their policies to the public. This public relations failure is costly both in terms of profit and in terms of caliber of employees attracted. After all, no one looking for a lifetime career would deliberately select a field of work which is held in such low esteem.

As further evidence of this failure to "sell" retailing to the public, a recent survey conducted among all graduating high school seniors in California showed that only 1½ per cent had ever taken even a single subject in the retailing field. Even more alarming, only 3 per cent expressed any interest in employment in retailing establishments. Only 3 per cent want jobs in stores; yet 25 per cent must eventually accept such jobs, since a fourth of our employed population works in this field! This means that over 20 per cent of these young people will take retailing jobs only with reluctance or after exhausting all other possibilities.

Analysis at the college level reveals the same pattern. Even among graduates of our specialized colleges of commerce, colleges set up specifically for training in business, retailing ranks very low as an occupational choice. An analysis of the figures from one college of where these graduates actually go to work shows that last year only 11 per cent accepted jobs in stores. The recruitment picture, spotlighted by these surveys, is certainly not promising.

What is the solution to this problem which confronts the average retailer? There is no one answer — no patent medicine remedy which will act as a cure-all. Certainly the evidence is overwhelming that a better public relations job must be done if the retailer is ever to get off this costly merry-go-round.

But good public relations start at home. The "public" forms its attitudes and beliefs on evidence obtained from personal experiences and from comments made by friends who are employed by the stores. In other words, *store employees* and the descriptions they give to their friends in the community largely determine how the "public" feels about stores. Therefore, the merchant must first "sell" his own employees on the benefits, values, and importance of his store. To do an effective selling job of this type the merchant must have something to sell — namely, an effective, *planned* personnel program. Which brings us back, full circle, to our starting point.

The days of expediency are running out. The pressure is mounting, and it will continue to rise in the field of retail personnel relations until such time as merchants generally accept the thesis that commercial enterprise can be profitable only through intelligent use of people. This thesis was accepted twenty years ago by industry, to its continuing benefit. All that is necessary is to provide employees with *planned* job security and job satisfaction — and to *let them know* about these plans. The resultant drop in the personnel turnover rate alone will more than pay for the time, effort, and dollars expended on the plans. It is the one sure means of getting off the personnel merry-go-round, and of raising employee morale, public esteem, and the level of applicants for careers in the retail field.

The retailer is the most important single link in our economic chain. Retailing can become a badge of distinction rather than a "last resort" job. The outcome is up to the individual retailer.

Television: Position and Outlook

DALLAS W. SMYTHE
Professor of Economics, University of Illinois

BY 1949 IT IS apparent to tens of millions of persons, in no way connected with the industry, that television is here to stay. It is a bewildering art, through which wrestling's "grunt and groan" form of theater entertainingly invades homes accustomed to other recreational pursuits. Television (or TV, as we shall hereafter call it) costs a lot to produce, as well as to receive, but offers attractive opportunities to many in direct or indirect employment, or as businessmen. It is a disturbing new industry in many ways: to other industries through its competition for consumer attention and money, to educators, to the Federal Communications Commission, and to legislators. It is loaded with problems and promise.

The task here is to appraise TV's position at the threshold of 1949 and to indicate some trends and problems in its future. So numerous and uncharted are the variables in TV that any precise statements as to its future must be taken as approximations. As Chairman Coy of the FCC puts it,

> Even men who are sinking millions of dollars of their own money into television are leaning heavily on intuition. It is a business in which there are no blueprints and in which everyone sees through a glass but darkly. It is a business that deals with sight but is played by ear.

To write on TV today implies either expert ability to predict, or temerity. But since almost everyone in the new industry has these qualities in varying proportions, the writer is in good company.

In contrast to the slow, fumbling beginnings of AM (amplitude modulation) radio twenty-five years before, TV was off to a fast start when it got the green light less than three years ago. Preceded by a long, skillful, and expensive public relations build-up, the industry boomed after March, 1946, when the FCC denied the Columbia Broadcasting System's request for commercial authorization to use color as well as black and white TV. This victory for RCA was understood to mean: Let's have black and white now; color will have to wait. Since then more than three hundred applications have been filed with the FCC for TV stations.

The hubbub attending TV has rather effectively blanketed out the attention given to a much greater increase in the number of FM (frequency modulation) stations on the air. Why? Basically, the reason is that TV has ridden the wave of an abundantly demonstrated consumer interest and that it appeals equally as much, if for varying reasons, to advertisers, to radio equipment manufacturers and dealers, and to enterprisers interested in staking out for themselves a portion of a very powerful and limited public domain — TV frequencies. For analytical convenience the problem may be approached in terms of several questions. First, where, how much, and what kind of service will there be? The logical second question is: What sort of effects will TV have?

Where, How Much, and What Kind of Television Service?

Where will the service be? At the end of the war there were 6 TV stations on the air; at the beginning of 1948 there were 19; as this is written there are 57 on the air, with others coming on at the rate of one to three a month. Competent estimates are that by the end of 1949 there will be between 100 and 120 stations on the air, and that by 1951 there will be 400, the service area of each having a radius of about 40 miles. All the present 57 stations are located in 30 metropolitan areas. They are listed in column (1) of the table. The largest group of TV communities — 12 in all — is in the Atlantic Coast tier of states. The North Central States have 8 TV communities. At present 23 states have at least one station each. The aggregate population in the areas now receiving TV service is about 48 million.[1]

Television is now broadcasting under a plan which allocates stations to 12 channels between 54 and 216 megacycles. The allocation plan, it may be explained, is a geographic spacing of station assignments designed for best use of the available channels, with regard to interference of stations on the same channels and on adjacent channels. In designing the present allocation plan for this "low" band, the FCC planned for about 400 stations to serve some 140 metropolitan areas. It was expected that about half the total population might obtain service with sets built to receive in this band.[2]

A nation-wide service for the whole population is not possible in the present state of the art in the low band. Experimentation has been going on for several years on the propagation characteristics of the "high" television band (475 to 890 megacycles), which the FCC had assigned to TV in 1944 with the express purpose of providing sufficient spectrum space to permit the development of a "truly nation-wide and competitive system."

Meanwhile, the interference experienced by the new stations which went on the air in the low band proved to be more serious than had been anticipated by the industry or the FCC. Consequently in September, 1948, the FCC "froze" its processing of new applications for stations, pending study by Commission and industry engineers of the best methods of combating propagation problems encountered. It was announced at the time that processing might be resumed at the end of six months or shortly thereafter. As a result of this freeze, some 313 applications for TV stations are in the Commission's pending file.

Applicants who had already been given their construction permits, however, were allowed to complete station construction and begin operations. At

[1] Counting population in metropolitan areas but not in remainder of TV service areas, according to the most recent Census data. For about half the communities data are as of 1947; for the remainder, as of 1940.

[2] A "band" consists of a number of channels assigned by the FCC for a particular radio service. The TV channels below 216 MC have been assigned for commercial TV service. The "high band," assigned for experimental work in both black and white and color TV, is between 475 and 890 MC. Because engineering standards have not been determined in this band, no allocation plan is yet prescribed.

PRESENT AND PROSPECTIVE TV STATIONS, FEBRUARY, 1949

COMMUNITY	Visible Supply of TV Stations			"Frozen" Assigned Channels and Applications	
	On the air (1)	Under construction (2)	Total (3)	Station assignments (4)	Applications in hearing (5)
ATLANTIC COAST					
Portland	..	..	..	2	2
Boston–Waltham	2	1	3	2	8
Fall River–New Bedford	..	..	..	1	3
Springfield–Holyoke	..	..	..	1	2
Worcester	..	..	..	1	2
Haverhill–Lowell–Lawrence	..	..	..	1	2
Hartford	..	..	..	1	3
New Haven	1	..	1	..	..
Waterbury	..	..	..	1	2
Providence	..	1	1	1	1
Albany–Schenectady–Troy	1	..	1	3	5
Binghamton	..	1	1	..	..
Buffalo–Niagara Falls	1	..	1	2	5
New York–Newark	6	1	7	..	..
Rochester	..	1	1	2	3
Syracuse	1	2	3	..	..
Utica–Rome	..	2	2	..	..
Atlantic City	..	..	..	1	3
Allentown–Bethlehem–Easton	..	..	..	1	4
Erie	..	1	1	..	..
Harrisburg	..	..	..	1	2
Johnstown	..	1	1	..	..
Lancaster	..	1	1	..	..
Philadelphia	3	..	3	1	2
Pittsburgh	1	..	1	3	7
Reading	..	..	..	1	2
Wilkes-Barre–Scranton	..	..	..	2	2
York	..	..	..	1	2
Wilmington (Delaware)	..	1	1	..	..
Baltimore	3	..	3	..	..
Washington, D. C.	4	..	4	..	..
Richmond	1	..	1	3	4
Norfolk	..	1	1	..	..
Huntington	..	1	1	..	..
Charlotte	..	1	1	2	3
Greensboro	..	1	1	..	..
Atlanta	2	1	3	1	3
Jacksonville	..	4	4	..	..

PRESENT AND PROSPECTIVE TV STATIONS, FEBRUARY, 1949 (continued)

COMMUNITY	Visible Supply of TV Stations			"Frozen" Assigned Channels and Applications	
	On the air (1)	*Under construction* (2)	*Total* (3)	*Station assignments* (4)	*Applications in hearing* (5)
ATLANTIC COAST (concluded)					
Miami	..	1	1	2	5
St. Petersburg	..	1	1	..	..
Total, Atlantic Coast	26	24	50	37	77
NORTH CENTRAL					
Akron	..	..	..	1	2
Bellaire–Wheeling	..	..	..	1	2
Cincinnati	1	2	3	1	1
Cleveland	2	1	3	2	5
Columbus	..	3	3	..	..
Dayton	..	2	2	..	..
Toledo[a]	1	..	1	2	2
Youngstown	..	..	..	1	3
Bloomington (Indiana)	..	1	1	..	..
Indianapolis	..	2	2	2	4
Chicago	4	..	4	3	5
Peoria	..	2	2	..	..
Rock Island–Davenport	..	2	2	..	..
Detroit	3	..	3	1	2
Flint	..	..	..	1	2
Grand Rapids	..	1	1	..	..
Kalamazoo	..	1	1	..	..
Lansing	..	1	1	..	..
Madison	..	..	..	1	2
Milwaukee	1	..	1	3	3
Minneapolis–St. Paul	1	2	3	2	1
Ames	..	1	1	..	..
Des Moines	..	..	..	4	5
St. Louis	1	..	1	5	6
Kansas City	..	1	1	3	6
St. Joseph	..	..	..	1	2
Omaha	..	2	2	1	2
Total, North Central	14	24	38	35	55
SOUTH CENTRAL					
Louisville	1	1	2	..	..
Memphis	1	..	1	..	..

PRESENT AND PROSPECTIVE TV STATIONS, FEBRUARY, 1949 (concluded)

COMMUNITY	Visible Supply of TV Stations			"Frozen" Assigned Channels and Applications	
	On the air (1)	*Under construction* (2)	*Total* (3)	*Station assignments* (4)	*Applications in hearing* (5)
SOUTH CENTRAL (concluded)					
Nashville	..	1	1	..	..
Birmingham	..	2	2	..	..
New Orleans	1	2	3	2	2
Oklahoma City	..	1	1	..	..
Tulsa	..	1	1	2	5
Dallas	..	2	2	2	4
Fort Worth	1	..	1	..	..
Houston	1	..	1	3	5
San Antonio	..	2	2	..	..
Total, South Central	5	12	17	9	16
MOUNTAIN					
Denver	..	..	..	5	6
Albuquerque	1	..	1	..	..
Phoenix	..	1	1	..	..
Salt Lake City	1	1	2	..	..
Total, Mountain	2	2	4	5	6
PACIFIC					
Fresno	..	..	..	4	6
Los Angeles	7	..	7	..	..
San Francisco–Oakland	2	1	3	3	6
Riverside	..	1	1	..	..
Sacramento	..	..	..	3	3
San Diego	..	1	1	3	4
San Jose	..	..	..	1	2
Stockton	..	1	1	..	..
Portland	..	1	1	4	5
Seattle	1	..	1	3	6
Total, Pacific	10	5	15	21	32
Grand total, United States	57	67	124	107	186

Source: Tabulation of TV grants and applications released by FCC as of January 1, 1949, with adjustments for changes up to February 28, and the valuable "Television Rates and Fact Book" published by *Television Digest and FM Reports* (Washington, D. C.).

[a] Toledo is shown as having a total of 3 channel assignments in an FCC release, published in *Broadcasting*, January 10, 1949, although the FCC Allocation Plan apparently provides only one channel.

the first of 1949, 67 stations are in this category. These provide the current additions to the ranks of operating stations. (See column (2) of the table.)

How many of the additional 313 stations may be accommodated on the low band cannot be decided at this time. The operating techniques which may be required of them and of the existing stations in order to provide a maximum of service on this band are also undetermined. Engineers are experimenting with various techniques. Synchronization of TV carrier signals is one means which might avoid interference to a certain degree. Directional antennas, of course, are another possible crutch. Within reasonable limits, engineering skill, backed up by the economic resources available to equipment manufacturers, may safely be counted on to reach a viable solution of the present impasse. It almost always does. Because of the momentum of TV, an end to the freeze sometime in 1949 is very probable.

While the freeze lasts, however, the immediate potential television service is limited to the 124 stations now on the air or holding construction permits. Where will these stations provide service? A total of 68 communities, including the 30 already served, will have television stations when the "visible" supply of stations are all on the air, as may be seen in columns (2) and (3). The additional TV communities will be distributed among geographic sections much as are those with currently operating stations. About nine million people will receive service in these 38 communities. Together with those now receiving service, therefore, about 57 million people, or about 40 per cent of the population, are virtually assured of TV service in the low band.[8]

Apart from the "visible" stations, a number of the 300-odd frozen applications are very likely to result in actual operating stations in the low band. About 24 communities besides those previously referred to will have no service (although eligible for it under the present allocation plan) unless the eventual "thaw" gives them some. In this connection see columns (4) and (5). All the applications from these communities were "in hearing" when the freeze hit them. They include cities as large as Denver, Des Moines, Fresno, Sacramento, San Jose, and Hartford. In these 24 communities some 66 applicants are tied up in hearings in competitive efforts to obtain about 38 licenses (which were available under the original allocation plan prior to the freeze). It seems altogether likely that after the freeze is over, most of them will be provided with some sort of service. The applications in hearing status also include about 120 located in some 30 communities which are already assured of at least some TV service. Probably many of these will be granted when the freeze is over. Among them will likely be some applications for additional stations in such cities as Boston, Kansas City, and San Francisco.

In summary, then, the present state of the technique indicates that no less than 68 and perhaps as many as 92 communities will have low-band TV

[8] See footnote 1.

sometime after the freeze is over.[4] On the basis of present indications, no less than 124 and perhaps as many as 231 stations may eventually operate in these cities.[5] While it is impossible to predict accurately the total number who will receive low-band service, it seems clear that this population will be virtually restricted to urban areas and, for the most part, to metropolitan areas.[6] Twelve states, with a total 1948 population of about 12 million, are not assured of having even one television station.

Will the rural and an appreciable portion of the urban population be able to look forward to receiving TV on the "high band," if not the low? Smaller cities than those now acquiring TV will get stations in the high band, if and when it is parceled out for commercial use. The radio manufacturers and the FCC are considering possible allocation plans and engineering standards in contemplation of such disposition of the high band within the next year or two. But so long as transmitters located on the ground are the basis of the allocations, full rural coverage by TV is hardly within the present perspective.

It may become technically feasible, however, to provide substantially nation-wide television service by the use of "stratovision" — a system of broadcasting from high-flying airplanes. In contrast to a service area of perhaps 40 miles from ground stations, stratovision is reported to serve hundreds of miles from a single airplane. According to its developers, a fleet of 20 airplanes could thus provide stratovision service to the entire country. Although only incomplete data are available, it appears that the cost of providing service by stratovision compares favorably with that of providing it by ground stations interconnected by coaxial cable or radio relays. The ultimate issue on which the possibility of stratovision appears to rest, however, is that of public policy. Already, men who in AM have opposed power in excess of 50 kilowatts have expressed opposition to stratovision on the argument that to give the operators of stratovision control over TV program service would be to vest too much political, social, and economic power in too few hands. In any event, however, stratovision might be licensed to provide service to selected, and otherwise unserved, areas.

Not the least of the uncertainties surrounding the kind of service the high band may provide is the question whether after all it will be available for *any* TV service. While it is true that the Federal Communications Commission has allocated the space between 475 and 890 MC for TV, its authority to allocate spectrum space is not unqualified. The President may make allocations for government services. And the armed forces are reported to be seeking this very portion of the spectrum for military uses.

---

[4] The 30 already served, plus 38 dependent on current construction, plus 24 where frozen applications in hearings now prevent even one station from operating.

[5] Counting present channel assignments as stations in the communities where all channels are frozen in hearings.

[6] Except for the rural audience which may receive service from near-by cities or from the small number of stations whose antennas are located on convenient mountains.

Assuming that TV is permitted to use the 475-890 MC band, however, when may we expect it actually to bring service to rural areas and small towns? Admittedly, there are technical problems of equipment design and performance in this little-charted area of the spectrum. These technical barriers are delaying the actual development of television in that area. Their solution is complicated by differences of opinion as to what kind of TV there should be in the high band. Is color TV feasible in that band in the present state of the art, or must color await the development of techniques in still higher frequencies? Would spectrum requirements for color permit sufficient channel assignments? Alternatively to either color or black and white under present standards, could the high band be engineered to obtain the advantages of higher definition black and white TV? Should the high band be reserved for either of these alternatives? In reaching decisions on such technical issues, public agencies necessarily must cope with the fact that the proposals for high band television as advanced by equipment manufacturers are naturally colored by their economic interests.[7] The momentum achieved by TV in recent months is likely to bring some solution to the high band problem before the end of 1949.[8]

The eventual timing of the shift in attention to the development of rural service, and of color in the higher portions of the spectrum, will also, of course, be influenced by public policy on such issues, as such policy is expressed through Congress and the FCC.

How much television service will there be? This question may be approached in terms of the number of various program services available to the viewer, in terms of the strength of the signals, in terms of hours per day of service, and, finally, in terms of the number of receivers.

In terms of the number of program sources available, 19 of the communities with stations now on the air have only one apiece. Four communities have two stations each, and seven have three or more stations. There are seven in Los Angeles, six in New York City (including Newark), and Chicago has four. When the stations now proceeding with construction come on the air, there will be 40 cities with one station each, 11 cities with two stations, and 17 cities with three or more.

In the early months of operation, stations frequently operate with less than their authorized power because of equipment problems. As time passes, therefore, the signal strength of the

[7] "Industry witnesses seem to be in accord on utilizing the high band — or a substantial portion of it — for the present television system. It seemed to be the consensus that high definition black and white or color would have to await future research and development. It is almost unnecessary to observe that such a position is compatible with their present interests." Chairman Wayne Coy, FCC, speech before Radio Executives Club and the Advertising Club, Boston, January 25, 1949.

[8] "I think it is extremely unfortunate that the demand for more channels is upon us before we are prepared to cope with it. The research and experimental work in the UHF [high] band lagged as we moved into the production of VHF [low band] equipment. I hope and expect, however, that the need for additional channels will be met before the current year is finished." *Ibid.*

stations on the air will increase up to their authorized limits, with a consequent improvement in the volume of service provided.

The hours-per-day of station operation are a fundamental aspect of the question of how much service television will provide. The FCC has adapted its rules on this feature of station operation to the practical economics of the industry. While all stations are licensed for unlimited time operation, they are required only to broadcast a minimum of 12 hours per week during the first 18 months of operation. For successive six-month periods of operation, the hours requirement rises progressively until, after three years of operation, a station is required to operate a minimum of 24 hours per week.

Over and above these minima, the hours of operation are left to station discretion. The determinations made by stations are generally the composite result of considering the costs of operation in relation to the station rate card and the ability of the station to sell its time to advertisers. Reserving, until later, consideration of the outlook for TV advertising, it is important here to indicate the bearing of networking on the quantity of television service. From an economic standpoint networking on TV is more necessary than on AM radio. Network distribution of programs permits the spreading of the very heavy program production costs of TV over a number of stations. Because TV operating costs are very high in comparison with AM radio costs, the reduction in costs resulting from networking permits TV stations to develop their service much faster than would otherwise be the case. Furthermore, national advertisers may more readily be sold time over a network of stations than over the stations individually. Until the FCC publishes some official cost data on TV it will not be possible to analyze these propositions statistically.

During 1948, TV networks were operated by four companies: NBC, ABC, CBS, and Allen B. DuMont.[9] Some of the intercity transmission was accomplished over the facilities of the American Telephone and Telegraph Company (both by coaxial cable and by radio relay), and some of it over private radio relay facilities of DuMont and Philco. AT&T had for some time been providing its facilities between New York and Washington to the TV interests on a free basis for experimental purposes. However, with its own widespread network of coaxial cable nearing completion of construction, AT&T in the spring of 1948 filed with the FCC tariffs to establish commercial rates for such service. Simultaneously, Western Union filed tariffs on similar service. These proposed rates were complained of as unreasonable by the Television Broadcasters Association, and by DuMont and Philco, and an FCC rate hearing was begun. About the same time, a related issue was joined by Philco and AT&T, first in the Philadelphia Federal Court, and later, at the Court's suggestion, before the FCC. Philco had sought to use the facilities of AT&T for TV program transmission

[9] DuMont, which is substantially controlled by Paramount Pictures, Inc., has been a pioneer in TV although not involved in AM networking.

between cities in connection with intercity facilities of its own. AT&T had refused to interconnect on the ground that it had facilities available for the entire "haul." The interconnection issue was joined with the rate case and hearings completed on the first issue, and at year's end this record was awaiting Commission action.[10]

While space does not permit analysis of the evidence in these two related issues, it should be noted that they have profound and long-run consequences for the size, structure, and rate of growth of the new industry. AT&T contended that even at the proposed rates the intercity relay of television programs would be noncompensatory. DuMont argued that small networks would be precluded from operating by the structure of the rates, which established 8 hours a day as the minimum quantity of time for which network facilities would be furnished, and by the level of rates. It may be noted that NBC, CBS, and ABC did not join in the attack on the rates, possibly because their TV networks will soon be large enough to permit economical use of the AT&T facilities under the proposed rate structure.

[10] Meanwhile this issue appears to have entered the complaint which the Department of Justice filed against AT&T on January 15, 1949. This complaint, according to the press, invokes the anti-trust laws in an attack on the common-ownership and control exercised by AT&T over its operating and manufacturing subsidiaries. *New York Times,* January 16, 1949.

At about the same time, AT&T filed amended tariffs with the FCC under which interconnection would be allowed until AT&T developed its facilities for serving any area at present unserved, but not thereafter.

Rapid progress was made during the year in actual network operations, largely as a result of a marked expansion of AT&T intercity facilities. On the Atlantic Coast, during 1948, the New York - Philadelphia - Baltimore - Washington chain of common carrier facilities was lengthened on the south to Richmond and on the north to Boston. In the Midwest, Chicago, Cleveland, Toledo, Detroit, St. Louis, Buffalo, and Milwaukee were linked together by AT&T. In mid-January, 1949, these two chains were joined between Philadelphia, Pittsburgh and Cleveland, creating a network of 30 stations in 17 cities.

Competing sharply for affiliates and intercity facilities, the TV networks have grown rapidly.[11] NBC, for example, had a four-station network in January, 1948; a year later it had 25 stations, and announced that its long-run objective was a national network of 154 stations serving a total of 85 million people. In 1948 its TV time sales were reported to be 1,000 per cent greater than in 1947. CBS began the year with one station and ended with a network of 24 stations; it projected a transcontinental network of 80 cities within three years. ABC in 1948 began operation of its own stations in New York, Chicago, and Detroit, and ended the year with a 20-station network. DuMont also greatly expanded its operations and by January, 1949, had a connected network as large as any of the others. All the networks resorted

[11] Because many stations affiliated with more than one network, the total of network affiliates exceeds the number of stations on the air.

to film recordings (known commonly as "kinescopings") of network programs in order to supply programs to affiliates beyond reach of wire lines or radio relay.

Expansion of TV depends on the relation of costs, rates, and the ability to sell time to advertisers. While this is true and helps to illuminate the economics of networking, it does not tell the whole story. Ultimately, the capacity of the individual station to serve its viewing public underlies its ability to sell time and to charge remunerative rates. Therefore a key fact which conditions the extent of TV service is the number of receivers within range of the transmitters. At present the public has over a million of these receivers, of which about 80 per cent were produced in 1948. Although this is but a small fraction of the number of AM radio receivers, it is more significant when compared with the number of families living in communities with TV stations. Moreover, the production and marketing of TV receivers is rapidly rising. Whereas in October, 1947, 29 manufacturers were producing home TV receivers, the list had grown to 66 by the end of 1948. Production in December, 1948, of 161,000 TV sets was five times the volume a year earlier. January, 1949, production fell to 121,000, which, however, quadrupled production in January, 1948. Industry estimates of production and sales of sets in 1949 range from 1.8 to 2.2 million. While these may be optimistic estimates, such an accomplishment is entirely possible if the allocations freeze is lifted in the spring and present levels of consumer income continue.

The service capacity of TV stations is of course more accurately gauged when the number of sets in use, the number of viewers per set, and their attitudes toward TV are considered. Thus far TV has registered in the order of twice as high a proportion of sets in use and twice as many viewers per set as AM. The attitudes of TV viewers will be considered later.

In the foreseeable future (i.e., one year), we might conclude, viewer interest may be multiplied several times, supporting the sale of more time and/or higher rates for the same time. This would speed the growth of the quantity of TV service in terms of stations on the air and hours of program service. Experience thus far indicates that, with more service available, viewer interest cumulates rapidly and a circular causal relation leads to an upward spiral in receiver sales and their consequent effects. The growth of station and network revenues which is expected, by providing the wherewithal, should make possible a vast improvement in the *quality* of TV service.

What kind of television will there be? As to the technical quality of the sight and sound which comes to the viewer from his receiver, the one sure prediction is that it will improve. Receivers with larger pictures will be available in greater quantity and at lower prices in the future. Improvements in the techniques of manufacture, larger-scale production, and greater competition among set manufacturers will all operate to this end. Similarly, the quality of the signals emitted by the transmitters will be improved by the stations. Substantial improvement may be looked

for in the technical quality of TV, therefore, such as occurred in AM radio quality after, say, 1924.

How one appraises the outlook for the *content* of the TV signal depends on a host of subjective factors. It depends on one's level of cultural tastes, and on one's social philosophy — specifically one's philosophy of the role of the mass media in our political and economic organization. Regardless of the individual's point of view on these issues, however, it is possible to describe the general shape of the future content of TV by reference to the purposes and practices of those who now are responsible for its programs.

Television is expensive to produce, costing several times as much as AM.[12] Because stations are normally interested in making profits, the hours of station service will be pretty much limited to the number of hours that can be sold to advertising sponsors. For example, the DuMont station in New York added 11 daytime hours (7 a.m. to 6 p.m.) to its operating schedule on November 1, 1948. It was able to do this because it started off with some 15 advertisers who responded to some special rate inducements good only for the first 13 weeks. By November 15, the station reported in the trade press that already the daytime segment was yielding more than sufficient revenue to offset out-of-pocket expenses. Their next problem was said to be

> . . . to produce the kinds of programs that will deliver the kinds of audiences that will get the original advertisers to renew their contracts at the full rate for time and talent when the trial period is over.[13]

This example also suggests a second generalization: that program content will be such as advertisers deem optimal for obtaining results, in relation to their advertising and selling budgets, and the effectiveness of other media. Just what kinds of program are optimal is not yet known; advertisers are experimenting with material. As recently as October, 1948, NBC's administrative vice president in charge of sales observed:

> The potential of the new medium is great. Its rapid strides in the last two years and the challenge of its commercial problems have practically forced the nation's major distributing organizations to experiment with it. Thus, we find such organizations as Proctor & Gamble, General Foods, Colgate, Philco, and the automobile manufacturers and distributors getting in on the ground floor. But they are not buying circulation. They are buying "know-how" at minimum costs. By getting into the picture early, they hope to establish a time franchise that will pay off in the long run.[14]

What kind of programs are advertisers choosing in their experimentation? A regular industry survey reports that for a week in January some 46 stations carried a total of 457 hours of commercial time.[15] "Sports" programs amounted to 39 per cent of the total,

[12] No reliable cost data are yet available for TV. Industry estimates of the investment in physical plant for a full-service TV station run from a bare-bones figure of $380,000 up to a million or more. By contrast, the average original cost of tangible broadcast property of the 300 regional unlimited AM stations in 1946 was about $133,000. Operating costs are said to bear a similar relation as between TV and AM.

[13] *Broadcasting,* November 15, 1948, p. 107.

[14] *Ibid.,* October 4, 1948, p. 62.

[15] "Rohrabaugh Report on Television Advertising," *Broadcasting,* February 21, 1949, p. 50.

and 151 hours of "sports" were broadcast by remote control. The second most common type was the "variety" program, which accounted for only 17 per cent of the total; "dramatic" programs were third with 12 per cent, followed by "news" (8 per cent); and "commercial announcements" came fifth with 6 per cent. "Education" and "discussion" programs ranked close to the bottom with 2.6 per cent and 1.4 per cent, respectively.

In terms of production technique, the 457 hours consisted of 41 per cent studio live, 34 per cent "remotes," 16 per cent studio film, and the remaining 9 per cent were a mixture of live, film, and slides. Lest this brief analysis leave the impression that programming neglects more sophisticated tastes, it is to be noted that in 1948 TV programming showed its promise in this direction. The American Broadcasting Company presented a full length telecast of Verdi's "Otello" direct from the stage of the Metropolitan Opera House, employing infrared spotlights to light the stage without distracting the theater audience.

The future content of TV programs is being shaped today. It is therefore pertinent to inquire what standards of taste are guiding its development. In a statement in lieu of an industry "code" issued by the Television Broadcasters Association, in October, 1948, the broadcasters recognized their obligation:

> . . . to observe the highest standards of good taste and fairness in the programming of their stations. The tremendous potentialities of television, combining as it does visual and aural appeal, create for the television broadcaster responsibilities far beyond those of any medium directed only to the eye or the ear. These responsibilities are heightened as television takes an increasingly important place in the American home.[16]

However, they conclude:

> The new techniques of combining sight and sound are engaging the creative talents and skills of the advertising world. But because the effects of these techniques both on television programming and on the television audience are as yet largely unknown, it is not possible or even desirable to attempt at this stage to formulate standards of practice.[16]

They recommend accordingly that broadcasters be guided by the standards of the aural broadcast industry and the motion picture industry "as far as they are applicable." While the dicta in this statement are certainly important, it is clear that, deliberately, no policy has been adopted. Moreover, one should not infer that men in the industry always talk in similar terms while addressing each other. Thus, the trade press carries a news story on an annual Eastern conference of the American Association of Advertising Agencies on November 15, from which the following statements are taken:

> Sex is frequently used in space advertising but not in radio, said one questioner, asking what about television. Mr. Griffin [Vice-president and group copy head, J. Walter Thompson Co.] gave as a good general rule to try to get away with as much as you can, mentioning that by use of good taste and skill radio advertisers frequently do many things they aren't supposed to do. Mr. De Rochmont [Producer of the "March of Time" films] advised everyone in television to take a strong stand against censorship from without but at the same time to do themselves what must be done to avoid it. "Use good taste all the

[16] *Broadcasting,* November 8, 1948, p. 66.

time," he commanded. He added that great as the danger of television becoming "potentially immoral" is, the greatest danger is that "you'll be potentially dull."[17]

Since commercial announcements are the essential matter of a commercial program, the perspective for TV commercials is of some importance. Here, too, experimentation is the rule. At one extreme are two agency executives whose words will bring relief to sensitive viewers. Mr. W. H. Case, vice-president of one agency, having spent $500,000 for an automobile account on television advertising in 1948, says:

> The television commercial can be less strident, more enjoyable because of the addition of eye to ear. . . . You can afford to move at a more leisurely pace. In fact, if you go too fast and heavy, you sacrifice effectiveness.[18]

Another agency criticizes the advertiser whose determination "to wring the last drop out of his allotted time succeeds only in most thoroughly annoying the viewer. . . . We . . . believe in the philosophy of keep it 'simple'."[19] At the other extreme we find an executive responsible for a two-hour Thanksgiving telecast saying:

> Eastern critics objected to the trip hammer frequency of the commercials . . . and I bow to their opinions on one count—there were too many. . . . However, I want to make it clear here and now: Our agency believes in putting "sell" in your "tele." It just can't be any other way . . . the total amount of commercial time in the two hours was 11 minutes and 45 seconds, which was still under the limit set by the NAB rules and regulations. . . .
> The Thanksgiving Day Holiday Star Vanities won applause everywhere as entertainment. That entertainment was made possible by an adequate appropriation by the client. And the appropriation was justified by effective and interesting commercials which sold the goods. It's high time that we advertising men stick to our guns and let the critics talk about entertainment. That's what they know. We know selling. Let's stick to what we know.[20]

The experimentation by advertisers, agencies, and stations with programming appears to be productive. While conclusive evidence of the advertising effectiveness of TV is not yet available, the experience of many advertisers has been very encouraging. In this connection, it is significant that studies in New York and Philadelphia suggest that TV-set ownership is concentrated in the families in the middle-income levels, with high-income groups possessing less than 20 per cent of the receivers and low-income groups having about 10 per cent.[21] In five months, the total number of advertisers using TV rose from 234 in June, 1948, to 912 in February, 1949. Between October and November alone a 50 per cent increase took place.[22] And the upward trend will continue.

What Sort of Effects Will Television Have?

Obviously, the creation of this new industry has the effect of giving the whole economy a "hypo," as the radio vernacular puts it. How strong a hypo is not known, for information on the extent of capital formation due to TV

[17] *Ibid.*, November 22, 1948, p. 69.
[18] *Ibid.*, January 3, 1949, p. 31.
[19] *Ibid.*, December 20, 1948, p. 31.
[20] *Ibid.*, December 13, 1948, p. 25.
[21] *The Pulse, Inc.*, quoted in Geyer, Newell and Ganger, Inc., *Television: Third Annual Report*, December 15, 1948.
[22] "Rohrabaugh Report on Television Advertising," *Broadcasting*, March 21, 1949, p. 38.

is not available. If, as some industry estimates have it, there will be 40 million sets by 1958, the consumers will have invested perhaps $10 to $15 billion in them. This hints at the magnitude of the economic effects of the new industry.

What effects will TV have on other media? More speculation centers on this question than on any other in industry circles. The aural radio, newspapers, magazines, and books within the home, and commercial recreation outside the home, now compete for a share of the leisure time of the American people. Moreover they compete with hobbies, conversation, participant sports, and noncommercial uses of leisure such as those connected with religious, social, and political activities. This complex pattern of leisure time use varies according to location, religion, race, income, age, and sex, and all other significant factors which differentiate the living habits of our people. TV is a competitive element in this pattern. Not enough research has yet been done to justify more than tentative and broad generalizations as to its effects. One study, however, suggests that

> Sports attendance suffers only slightly, while movie going and reading decline about one-fifth. Other commercial entertainment drops off about one-third, while radio listening is cut nearly in half.[23]

The same study tentatively suggests that radio listening and movie attendance on the part of TV set owners do not gain substantially after the novelty wears off. And another study finds that average radio listening for TV-owning families decreased an average of 57 per cent, with 81 per cent of the families reporting a decrease of more than 40 per cent in radio listening.[24]

It may help in thinking about this question to remark that other uses of leisure time will be affected on two levels, and the effects on these levels may, or may not, reinforce each other. Specifically, the first and more obvious level of competition may be called the "program appeal" level. Here the quality of the program appeal of the various media and the viewer's habits and interests in non-media uses of leisure will be competing. The second level arises out of the nature of TV. It is generally believed to be a jealous mistress of the patron's time. One may not, it is argued, read, cook, sew, or converse effectively while watching TV. To the extent that this exclusivity of attention is realized in fact, it elbows other claimants out of the viewer's activities. This factor now appears to be working strongly in favor of TV, but it could backfire. In other words, other media and competitors for leisure time may in self-defense make more effective appeals to consumer attention than they now do. When that happens, TV will have to be good enough to hold *all* of the viewer's attention. It cannot, apparently, settle for ears only, or eyes only.

Leaving the scanty research evidence, what do the experts think will be the effects? In the first place, an impressive consensus exists that TV makes pos-

[23] Thomas E. Coffin, Hofstra College, Hempstead, Long Island, quoted in *Broadcasting,* November 15, 1948, p. 10.

[24] Advertest Research, New Brunswick, N. J., quoted in *Broadcasting,* December 20, 1948, p. 42.

sible something like a millenium. Thus, Chairman Coy of the FCC tells the Theater Owners of America, in convention assembled:

Eventually there will be one or more television sets in every one of the 39,000,000 homes in America. . . .
I foresee the day when television will be the most powerful instrument of communication ever devised, the most universal and most effective purveyor of education, information, culture and entertainment.[25]

And Mr. James D. Shouse, President of the Crosley Broadcasting Corporation, says:

Within five years, it is entirely conceivable that television will have become an integral part of the lives of 20 to 30 million families . . . the influence upon their daily habits, their thinking and their concepts and philosophies will be severe — so severe, indeed, as to be literally revolutionary.[26]

A concurring point of view from the motion picture industry rounds out our picture when Mr. Spyros Skouras, President of 20th Century-Fox Film Corporation, says:

We are dealing with no midget marvel of the moment. We have on our hands a mighty giant and until it is fully grown and developed it will plague us and upset us [but eventually] the zenith in entertainment will be reached.[27]

It is also generally agreed that TV will eventually replace most AM radio. Already its effects on AM are apparent in major metropolitan markets like New York and Baltimore, where TV has been on the air for at least several years. Thus, equipment manufacturers state that already sales of high-priced AM radio receivers have suffered from the competition of TV sets. The *Baltimore Sun,* with a TV station and an FM station on the air, turned back to the FCC a perfectly good construction permit for an AM station, explaining the action this way:

While we were looking for a new AM transmitting site, the FCC released one of its useful economics reports. . . . Average broadcast income from the 11 stations then on the air (in Maryland and Delaware) was $134,993. This caused us to wonder what the average income might be if the 53 stations now authorized, including three television stations, were placed in operation in these two states. . . .[28]

While in the not too distant future TV may be expected to supplant most aural radio in urban areas, the continuation of both FM and AM aural radio in rural areas and small communities seems assured. Meanwhile, the transition from AM to TV in the large urban areas is as yet hardly started. Thus far, NBC reports proudly that a substantial number of its TV advertisers are new users of radio. The AM industry obviously hopes that it may sell TV advertising as a competitive form of advertising to that of newspapers and magazines as much and as long as possible. In that way, the segment of the AM destined for replacement may pay profitably for its own demise.

What of the effect on theaters? As previously suggested, it is likely to be heavy both on the legitimate stage and on motion picture theaters. How will movies adjust to TV? Probably by joining it — in several senses. Serious ef-

[25] Address to the Theater Owners of America, Chicago, September 25, 1948.

[26] Address to the National Editorial Association, Chicago, *Broadcasting,* November 22, 1948, p. 29.

[27] *Broadcasting,* January 10, 1949, p. 64.

[28] *Ibid.*, p. 65.

forts have been and are currently being made by large motion picture producers to acquire TV stations. At present, Paramount Pictures is involved with the anti-trust laws over this matter. In another sense, Hollywood is beginning to orient itself towards TV. Many small new enterprises are now beginning to produce films specifically for this purpose; and in December Hal Roach, a pioneer in motion picture production, announced his withdrawal from production for theater consumption, and the formation of a new corporation to produce films for TV. Lastly, attention is being paid to the possibilities of installing large screen viewers in theaters and programming theaters with part film and part TV. Technically, there is no barrier to this. However, strategic positions built on patents and legal precedents have impeded the development of theater use and presumably still do so. For example, early in 1949 a consent judgment was entered against three film companies controlling TV patents. Under the decree, there will be released for industry use patents and processes on the "supersonic" and "skiatron" systems of TV transmission and reception. The TV systems in question were described as permitting

> . . . the use of large-size viewing screens suitable for homes, schools, and motion picture theaters. Successful exploitation of these patents would therefore open up new possibilities in the entertainment and educational world.[29]

Other serious legal issues which remain to be resolved relate to "unauthorized pickups" of telecasts. Litigation and negotiations are currently under way on some of these issues.

The remaining mass media — newspapers, magazines, and books — apparently have less competition to fear in the near future from TV than has AM radio.[30] Very little information is available as to what they propose to do about it.

Already, however, commercial sports have evidenced grave concern over the effect TV will have on them. If it permits the whole nation to become "one vast knothole gang," to borrow a figure of speech from Chairman Coy, who is going to pay for boxing, football, and baseball? The national commissioner of the National Boxing Association, for example, recently disclosed that it is studying the effect of TV on boxing, with a view to negotiating a policy with the broadcasters. The argument is that telecasting of boxing destroys boxing clubs wherever the telecast is received.

[29] Herbert A. Bergson, Assistant Attorney General. The three defendants, Paramount Television Productions, Inc., General Precision Equipment Corp., and Scophony Corporation of America, were charged in the complaint in December, 1945, with conspiring with Scophony, Ltd., to monopolize the manufacture and sale under TV patents developed by the British corporation. The first two companies were charged with refusing to exploit these patents themselves, and with refusing to permit Scophony Corp. of America to exploit them. According to a statement by Arthur Levey, Scophony president, the supersonic cell "will make available — both in homes and in theaters — large screen video reception in varying sizes vastly superior in quality and substantially lower in cost than that now offered by the cathode ray tube method." *Broadcasting,* January 17, 1949, p. 52.

[30] But the New York State Publishers Association was recently advised by one publisher that TV would take from them "considerable national advertising." *Broadcasting,* January 24, 1949, p. 37.

For instance, if a good fight is televised from Washington, the fight club in Newark or Richmond Hills or Pawtucket is badly dented.[31]

It is argued that, whereas radio broadcasts built up boxing, TV approximates an eye-witnessing. Similarly, the athletic director of Georgetown University argues that TV is the biggest threat to college athletics, especially football, and that the only recourse for the universities is to prohibit telecasting. While radio did whet the curiosity of listeners and contributed to filling stadia, he feels that ". . . television doesn't whet curiosity. It satisfies it and leaves nothing to the imagination."[32] The result, so the argument runs, will be that universities and colleges will lose the income from their only profitable sport.

When that happens, all college sports will be doomed. For football pays for all the others — for from 8 to 16 sports.[32]

It is probable, however, that some satisfactory price will be reached in bargaining between TV interests and the producers of the TV-able sports, so that major colleges and universities will not find their athletic revenues eliminated. The impact of TV thus might fall principally on the places where major sports are less profitably commercialized. It will also have an impact, as yet unmeasured, on manufacturers of products used in hobbies, such as photographic supplies, and on night clubs, and similar commercial recreation.

There may be effects which are potentially more grave than those mentioned above. TV is notably expensive to operate, and the number of possible stations and networks is severely limited by engineering as well as economic factors. Previously, ownership interests in standard broadcast, motion pictures, and newspapers were substantially distinct although considerable overlapping existed. Each of these types of interests will be heavily involved in TV. With this association, something new has been added. In addition, Richard W. Hubbell, a television management consultant, states, perhaps overdramatically:

The dominance of the standard radio broadcaster in television is being challenged. Some of the most impressive new television projects have been organized by men who have made their millions in the oil business, in the cattle business, in publishing and in diversified manufacturing enterprises.

The influx of new money typified by these people will bring about an ownership and management revolution in the broadcasting industry in the next 18 months to two years. . . . Within the next decade television will not only create a number of new millionaires but will also become the prime mover of the economy.[33]

In brief, there is in prospect a new and greater concentration of control of the mass media of communications focusing on the most potent form of the art yet developed.

Finally, one may ask what is implied by TV with respect to the relation of the individual to the whole society? Will viewers become "addicted" to TV? Is it possible that they will become passively habituated to accepting predigested attitudes as a substitute for thinking and talking about problems? What effect will the regular exposure of a majority of the population for an average of several hours a day have

---

[31] *Broadcasting,* January 10, 1949, p. 34.
[32] *Ibid.,* December 20, 1948, p. 30.
[33] *Ibid.,* January 10, 1949, p. 64.

on the individual's capacity for the exercise of his own, whole personality in thought and action? Will TV have an integrative or a disintegrative effect on individual and family life? What is its relation to the problems of minority groups? Will it have a constructive or a destructive effect on the processes of democratic government in dealing with local, regional, national, and international problems? What becomes of the theory of the public service responsibility of the broadcast licensee? Is a new national policy on communications called for? If so, what kind of policy should it be?

The Economics of the "Pegs"

George W. Coleman

Economist, Mississippi Valley Trust Company, St. Louis

SOME MEMBERS of the financial community are currently engaged in discussing the advisability of continuing the Federal Reserve System policy of "pegging" the prices of long-term government bonds. Although most discussions of financial affairs are to be found only in the financial pages of daily newspapers, this discussion has been reported from time to time on the front pages, and it will receive more attention later.

The discussion revolves about the advisability of retaining the "pegs" on the long-term securities, since there seems to be substantial agreement that short-term rates should be permitted to rise somewhat higher. The long-term securities referred to are, primarily, the 2½ per cent bonds. Furthermore, apparently only the long-term securities which are ineligible for bank ownership are "pegged." While the Federal Reserve System has on occasion purchased other securities, it is supporting "for the foreseeable future" these long-term bonds at a 2½ per cent level. Actually, the current support price is slightly higher — 100¼ — for the longest issue. There is, of course, no commitment to maintain this premium, since it results in a yield of slightly less than 2½ per cent. In this controversy, the intermediate-term securities have not been considered, but it is generally assumed that they will fluctuate in relation to the long- and short-term securities.

Although a great many additional factors have been discussed, the basic arguments revolve about the effectiveness of a change in interest rates as a method of controlling fluctuations in prices and industrial activity, and the probable results which might follow from permitting government securities to fall below par.

The leaders of the group advocating the abandonment or the lowering of the "pegs" are Thomas I. Parkinson, President, Equitable Life Assurance Society of the U. S.; R. C. Leffingwell, Chairman of the Board of J. P. Morgan & Company, Inc.; and the Committee on Public Debt Policy. The National City Bank Monthly Letter has criticized the "support" program, and many other financial commentators are not in complete sympathy with it.

The Case Against Pegging

It would be difficult to present the complete argument of each of the opponents of the "support" program, but their main argument can be summarized in the following way: The "pegging" of the government bond market is inflationary, since the Federal Reserve System is almost the only buyer. Purchases by the Federal Reserve System tend to expand bank reserves and thus to lay the foundation for further bank credit expansion. They argue further that if the "pegs" were removed, and bond prices were permitted to find their natural level, other savers would come into the market and it would be supported at some lower

figure by these savers without expanding bank credit.

Very few of the advocates of removing the "pegs" are willing to go so far as to insist upon an absolutely "free" market. Many concede that an absolutely "free" market would be too demoralizing. Instead, they argue that the Federal Reserve System should restrict its efforts to the maintenance of an "orderly market." An "orderly market" is somewhat difficult to define but presumably it means one in which a buyer will always be available and in which prices will not drop precipitously. In addition, there are some who advocate that the "peg" should be lowered to 98 or 97 for the long-term bonds. This would, they say, cause selling to "dry up" because institutional investors, principally insurance companies, would be unwilling to sell securities at a loss in order to buy others.

Those who argue for the abandonment of the "support" policy basically are arguing for the restoration of the traditional function of the interest rate. According to classical monetary theory, the interest rate was conceived to be the factor equating the demand for and the supply of lendable funds. According to this theory, if the interest rate advanced, borrowers would be forced out of the market; hence, the level of investment in new capital equipment would decline. An investment in a new capital good which might be estimated to be profitable if money could be borrowed at 2 per cent might have to be abandoned if the interest rate were raised. Consequently, the classical economists argued that a rise in the interest rate would tend to lower the volume of investment in new capital goods. This, in turn, would decrease the demand for goods and reduce inflationary pressures correspondingly. According to this theory, a rise in the rate of interest would also encourage saving and thus tend to reduce the demand for goods on the part of consumers.

This theory can be applied to the "support" program. As Leffingwell recently stated in *Fortune,* "The Federal Reserve bond buying operation has kept excess money afloat. Too much money, too easy, too cheap, leads people to borrow too much and spend too much."[1] The present rate of interest is so low that borrowing is tending to exceed saving. A higher rate of interest might discourage borrowers and encourage saving. It is, moreover, important to realize that, according to this argument, a change in the interest rate on government securities will affect directly the corporate and municipal bond markets.

It is not surprising that criticisms of this suggested policy have been made. For example, it has been asserted that, if the Federal Reserve System should attempt to establish an "orderly market" at a level above that at which other buyers would appear, the inflationary effect in terms of expanding bank reserves would be nearly as great as the expansion which results from maintaining the present "pegs." The response of other investors (to be discussed later) might cause a substantially greater increase in the volume of bank reserves, however.

[1] R. C. Leffingwell, "How to Control Inflation," *Fortune,* October, 1948, p. 91.

The argument that a price slightly below par would discourage the selling of government securities is not entirely conclusive. John H. Grier, Vice President of the First National Bank of Chicago, summarized this argument in a speech in Des Moines when he said, ". . . the insurance companies might prove reluctant to take much of a loss on the sale of governments in order to acquire other assets with a higher degree of credit risk." He cited the fact that insurance companies have about $1.07 in assets for every dollar of liabilities, and he argued they would be unwilling to take much loss. Whether this is true or not is problematic. On strictly formal grounds, it can be stated that the price of other bonds would probably fall more rapidly than those of government bonds if the "pegs" were removed. If this did occur, the incentive to shift to higher-yield securities would be greater than it is now. Whether the other bonds would prove as attractive at the lower levels, because of changing business trends, is unpredictable. Whether investors would attempt to shift from government securities to corporate securities at low prices would depend upon the relative levels of interest rates and the expected trend of business activity. If business expectations were favorable, the shifting of funds from government securities to corporate securities might take place on a large scale. If business expectations were unfavorable, a shift of funds from corporate to government securities might take place. Since, to repeat, the price of corporate bonds would probably fall farther than the price of government bonds, a shift from corporate to short-term government securities might also result from a desire to minimize losses. While the response of the securities holders to a move to lower the price of government securities is not predictable, it is obviously not limited to a single course, as those who advocate lowering or eliminating the "pegs" imply.

The Case for Pegging

In addition to refuting the arguments of those who oppose the "support" program, the advocates of the retention of the "pegs" advance several arguments in support of their position.

In a recent Congressional hearing on inflation, a number of government officials stated that the effect of the removal or lowering of the "pegs" would be disastrous. They argued that the size of the Federal public debt is so great that it would be unwise to attempt to permit it to fluctuate freely. They implied that, quite apart from any discussion of the desirable level of interest rates, the failure of the Federal Reserve System to provide a market for government securities would result in complete demoralization of the market. This is true simply because there is no other agency that has the power to buy and sell government securities in a volume sufficient to meet the needs of the money market. To abandon the "pegs" under these circumstances would mean by its very nature, they argued, the abandonment of the government securities market to needless chaos.

Whether the abandonment of the "pegs" would produce chaos and quotations far below par is, of course, the

point in dispute. The probable response of some investors has been discussed earlier but, if the marketable securities did fall to the low 80's as occurred in 1920, the proponents of the "support" program fear that the holders of demand securities — Series E, F, and G bonds — would become panicky and present them for redemption on a large scale. While liquidation might, it is supposed, be general, it would probably be heavier in the case of the Series E bonds than for Series F and G bonds.

This fear probably arises from the experience of the Treasury Department with War Savings Certificates after World War I. It will be recalled that the sale of War Savings Certificates started in December, 1917. After the war, no attempt was made to support the government securities market, and some bonds declined sharply. In the period from May through August, 1920, a number of government issues fell to the low 80's. Sales of War Savings Certificates were reduced sharply in the fiscal years 1920 and 1921 while redemptions increased. No data are available showing whether the proceeds were used to buy securities in the open market, were spent for consumers' goods, or were hoarded.

Those who regard this fear as exaggerated point to the fact that the yield on Series E, F, and G bonds rises sharply in the later years of the life of these securities. Consequently, it is argued that yield-conscious investors will hold their securities. For example, although a Series E bond yields 2.9 per cent over its entire life, the approximate yield over the last five years is 4 per cent. In other words, in order to justify on a yield basis the redemption of a Series E bond held five years, it would be necessary to purchase a five-year bond yielding more than 4 per cent. A great proportion of the smaller denomination securities in this series has already been redeemed, and the current holders, it is argued, are primarily investors who would compare the yield to maturity with the yield obtainable in the market, before tendering them for redemption. If this appraisal is correct, then the much-feared surrender of demand obligations for cash might not reach the magnitude forecast.

If, on the other hand, a decline in government securities below par led to the large-scale presentation of Series E, F, and G bonds for redemption, the monetary consequences might be extraordinary. On July 31, 1948, there was outstanding \$52.2 billion in Series E, F, and G bonds. If any large portion of these bonds were presented for redemption the Treasury would be compelled to borrow money, since tax receipts and bond sales would not provide sufficient funds to retire these bonds. The Treasury can borrow directly from the Federal Reserve System \$5 billion, and the remaining amount would probably have to be borrowed from the "open market" through the issuance of Treasury bills. In effect, this would mean indirect borrowing from the Federal Reserve System. The expansion of Federal Reserve credit and, consequently, of member bank reserves, might be very great. Of course, the sellers of savings bonds might utilize the proceeds to purchase marketable securities below par. If the Federal Re-

serve System would consent to sell its long-term securities below par as an "open market" operation, member bank reserves would be reduced, but the possibility of reducing bank reserves in this manner is negligible.

In short, in an absolutely free market the abandonment of the "pegs" might result in a tremendous expansion of bank credit. While it is generally assumed that the abandonment of the "support" program would lead to a sharp deflation, even that is not certain. Public psychology is difficult to forecast and the result might be different from that supposed. With government expenditures remaining at a high level and with consumer income at a high level, it might be concluded by some that the vast expansion of bank credit would be the prelude to still further inflation and a moderate retreat to real goods might take place.

In answer to those who argue that the "pegs" should be removed and that the interest rate should be permitted to seek its own level, the following argument has been made by those who argue for the maintenance of "pegs." There is actually considerable question about the effectiveness of the interest rate in accomplishing the purpose attributed to it by the classical theorists. This is probably more true in cases where the change in the interest rate is relatively small, for example, an increase from 2 to 3 per cent. Inductive studies show that businessmen do not primarily consider the level of interest rates in undertaking ventures. This is certainly true in the case of short-term borrowing, and even in the case of intermediate-term borrowing the interest rate is not overly important as a determining factor. Intermediate-term money is frequently borrowed for new machinery and equipment. Here, the risk of obsolescence is so great that, relatively, changes in interest rates appear unimportant. In the case of long-term investments in public utilities and housing, the interest rate is a more important factor. At best, however, a moderate upward adjustment in the level of interest rates, it is stated, would probably not affect borrowing appreciably.

Furthermore, it can be shown that the volume of savings is determined primarily by the level of consumer income and also by its relative distribution among income classes. How effective the interest rate would be in inducing additional saving is, of course, not determinable. It seems reasonable to assume, however, that a change from 2 to 3 per cent would not cause a great increase in the volume of saving. Under these circumstances it is possible to question the effectiveness of an increase in interest rates as a method of reducing the level of investment in new capital goods or increasing the volume of savings.

It is, of course, true that in the past a rise in the rate of interest has frequently been followed by a decline in the level of business activity. Those who argue that the interest rate is ineffective as a method of control assert that a rise in the rate of interest frequently is a symptom and not a cause. They attribute the end of the speculative boom to the fact that the monetary system has reached the ultimate degree of expansion and, consequently, the in-

flationary forces have been completely exhausted. In other words, the banking system was completely loaned up. For them the interest rate itself only reflects the fact that additional credit is not available.

Perhaps, within the confines of these conflicting claims and assertions a monetary policy can be found which will operate to curb the inflationary forces without setting off a chaotic dumping of securities or the surrender of securities on a large scale for redemption. Monetary authorities have not been slow to advocate various schemes for special reserves and other arbitrary measures to control credit, and there is some support for those plans. But, fundamentally, most of these plans are makeshifts designed to limit the consequences of inflationary policies adopted elsewhere in the economy, particularly in the governmental sector. Such plans are, moreover, dangerous because they tend to obscure the fact that the causes of inflation arise in other sectors, and the adoption of one or more of these plans will have little effect. Inflation still remains a serious problem, but it must be attacked at its source, namely, unsound fiscal policy and unwise wage policy. When appropriate measures are adopted in these fields, then measures to restrict bank credit might be effective, but not until then.

In the last few weeks pressure upon the government bond market has diminished, since present holders are no longer selling aggressively and in some cases are re-investing. Quotations have risen above the "pegs" in most cases, but it would be a mistake to argue that a "free" market exists for government securities. Even though the bonds are selling above the "pegs," an announcement of the removal of the "pegs" would not go unnoticed by the market. While the Federal Reserve System is currently not compelled to buy securities at "support" prices, the question of the advisability of retaining the "pegs" is still discussed. Thus far, no completely satisfactory answer has been found.

The Federal Budget for 1950

EVERETT E. HAGEN

Professor of Economics, University of Illinois

MONEY, IT HAS been observed, "makes the mare go." So it is that almost every major policy of the Federal government is summarized in the request for funds which the President sends to the Congress early each January.

Two years ago, the President asked for $35 billion plus for fiscal 1948 (the year ending on June 30, 1948), and a Republican Congress gave him not quite $34 billion. Last year for fiscal 1949, the same Congress acquiesced in his judgment that expenditures must rise, and gave him $40 billion. Last month, for fiscal 1950, he sent Congress a request for almost $42 billion.

The $34 billion budget of fiscal 1948 marked the third annual step in the postwar descent from the wartime expenditure peak; then the trend turned upward again. The 1950 budget, the second successive increase, makes it clear that the decline in war expenditures has been more than matched by the rise in postwar expenditures, and that for the indefinite future Federal expenditures in the forty billions must be regarded as normal.

True, Congress may cut some of the President's requests; but, on the other hand, some requests which will add to the budget are yet to be made. Funds for military aid to the "Western Union" — that is, to western Europe — are yet to be added to the total, and other smaller supplementary requests will no doubt also be made. The Eightieth Congress, politically hostile to the President, announced its determination to cut the 1949 budget to the bone; and cut it did, so far as it thought desirable. But when it had made its alterations in the original budget, and had considered also the supplemental requests for funds, and had added programs of its own, the budget as a whole came out from Congress larger than it had gone in. Unless the present Congress, of the President's own party, finds more weak spots in the budget than did its predecessor, the budget in its final form will again be larger, not smaller, than the original (incomplete) request.

Budgets in the $40-billion range are now "normal." To an individual, even *one* billion is such an incomprehensible amount that it is easy to gain an exaggerated impression of how great a sum $42 billion really is, in comparison to the size of the American economy. It is (only) seven times as much as American consumers will pay to the automobile industry for the purchase of automobiles — new and used — this year. Yet, even in its proper perspective, $42 billion is a great deal of money. It would purchase a new popular-priced automobile for each family (and each single individual supporting himself), every second year. It is about two-thirds as much as we will spend for food this year, if high incomes continue, and is close to one-sixth of the value of all the goods and services being produced in our economic system.

In a sense, this is not a normal peacetime budget, for it contains large

international expenditures which are not permanent, and huge defense expenditures which, it is to be hoped, need not be continued indefinitely. But in the years immediately following 1950, defense expenditures will rise, not fall, because of programs already authorized. Other programs too will rise during the early years of the next decade — for example, the housing programs which the President has proposed. All in all, if a budget above $40 billion is not normal, then it can only be said that it will come to seem normal as a succession of such budgets makes us accustomed to them.

The 1950 budget, like that for 1949, seems abnormal because it is such a startling departure from the prewar trend. As Chart 1 shows, expenditures in fiscal 1950 will be almost five times as great as those in fiscal 1939, the last year before war broke out in Europe.

This tremendous increase from prewar to postwar is not an unprecedented development. *Each great war in the nation's history has marked an apparently irreversible step to a new, greatly expanded concept of the scope of governmental activity.*

There is something about a war — any major war, apparently — that renders forever obsolete prewar standards of the scope of governmental activity. Federal expenditures during the years just preceding the outbreak of the Civil War were fairly stable at about $70 million per year. Never after the war were they less than 7 times as great. Annual expenditures just prior to World War I were approximately $700 million. In the economy period of the Coolidge twenties, they remained on a plateau more than 5 times as high. The evidence of history and the nature of public attitudes that are molding

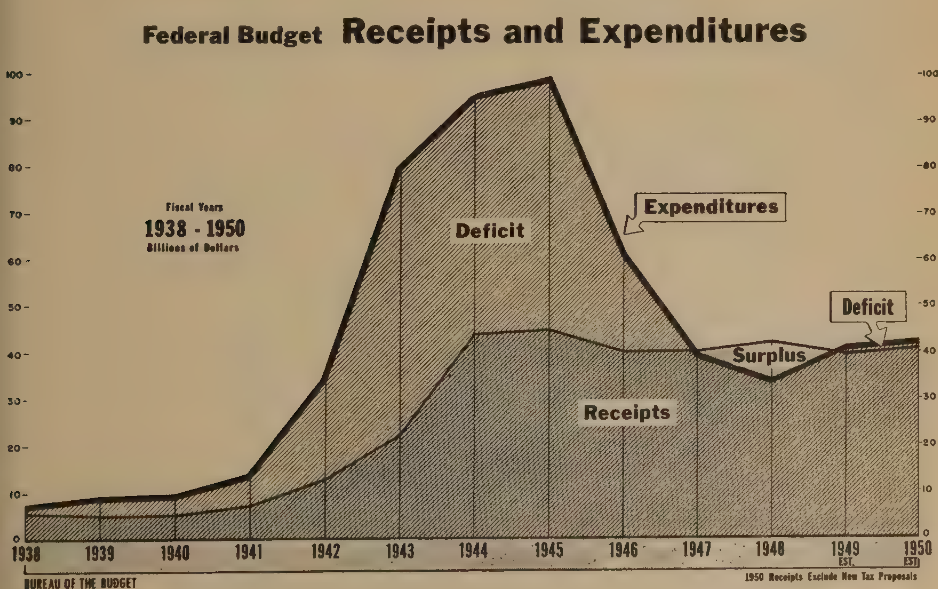

CHART 1. Federal Receipts and Expenditures, 1938-1950

governmental action at present point to a common conclusion: Federal expenditures after World War II would be at roughly their present level, no matter which political party had been in power since V-J day.

The Break with Prewar Traditions

A brief item-by-item comparison of prewar and postwar expenditures will indicate, even more forcefully than does this general historical comparison, the reasons for considering the greatly increased budget level a permanent one. The accompanying table shows Federal expenditures, classified by the functions which they serve.

For an analysis of the change in expenditures from prewar to the present fiscal year, it is illuminating to separate the non-war-connected expenditures from the expenditures which by and large result directly from postwar or from the aftermath of war, or which are for defense against possible future war. In the war-connected group are included, in addition to national defense expenditures, those for veterans' services and benefits, international expenditures, and interest on the public

FEDERAL EXPENDITURES BY FUNCTIONS
FISCAL YEARS 1939, 1949, AND 1950
(Dollar amounts in billions)

Function	1939 (actual)	1949 (estimated)	1950 (proposed)	Percentages: 1949 of 1939	Percentages: 1950 of 1949
National defense	$1.1	$11.8	$14.3	1,094	121
International affairs and finance	*	7.2	6.7	37,995	93
Veterans' services and benefits	.6	6.8	5.5	1,216	81
Interest on the public debt	.9	5.3	5.4	566	102
Social welfare, health and security:					
Direct and work relief	3.1	*	*	...	...
Other	.9	2.0	2.4	222	120
Natural resources not primarily agricultural	.2	1.6	1.9	755	115
Agriculture	1.2	1.8	1.7	151	92
Transportation and communication	.5	1.8	1.6	343	90
General government	.6	1.2	1.2	213	103
Education and general research	*	.1	.4	193	487
Housing and community facilities	−.1[a]	.3	.4	...[a]	111
Finance, commerce, and industry	.1	.1	.1	196	105
Labor	*	.2	.2	1,673	102
All functions	$9.0	$40.2	$41.9	447	104

* Less than $50 million.

[a] Receipts from repayment of earlier loans and advances to states and localities exceeded housing expenditures in 1939; hence, no percentage can be calculated.

debt. The classification into the two groups is arbitrary, since the influence of war ramifies throughout the budget; but it is nevertheless a useful distinction. Chart 2 illustrates this grouping of expenditures.

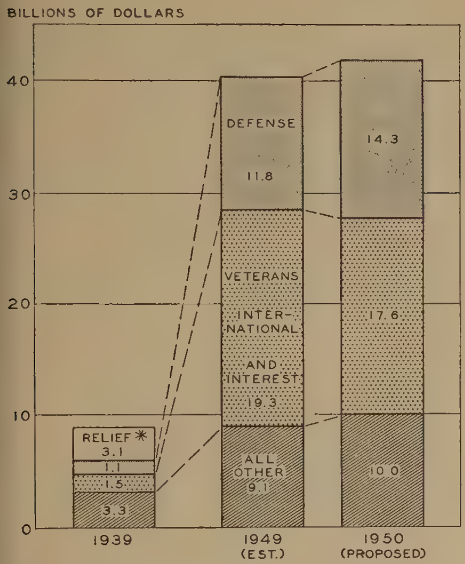

CHART. 2. Federal Expenditures by Function Groups, 1939, 1949, 1950

A major reason why World War II swelled the Federal budget is easy to see. It lies in the fact already noted that of the $40 billion which is being spent in fiscal 1949, more than three-fourths is war-connected — that is, is for national defense, veterans' services and benefits, international expenditures, and interest on the public debt.

As the table indicates, the amount for these four purposes in fiscal 1939 was $2.6 billion. The United States showed its disregard for world affairs, in which it should have had a position of leadership, by spending only $19 million for international affairs. For the veterans of twenty years earlier, we were spending what seemed the handsome sum of $559 million; for interest and for defense, in the neighborhood of a billion dollars each. The 1949 total of $31 billion for these four purposes is 12 times the 1939 sum, and in fact 3½ times the total 1939 budget.

Expenditures in fiscal 1949 for all other purposes are not far from 3 times the corresponding expenditures of 1939 (omitting prewar relief expenditures from the comparison). Expenditures in 1939 for all non-war-connected purposes other than direct and work relief were $3.3 billion; 1949 expenditures are $9.1 billion. A large part of the increase, of course, is due to the rise in prices, which has swelled both public and private expenditures (and incomes). But a purpose-by-purpose comparison of Federal expenditures in 1939 and in 1949 will indicate that many basic increases due to other causes have also occurred. The large increase in non-war government expenditures can be understood only in terms of the specific programs initiated or expanded and the needs they were designed to fulfill.

In the field of social welfare, health, and security, a $550 million increase in grants to the states for assistance to the aged and other special groups, which almost doubles these expenditures, is accounted for by increases in level of grants and in the number of the aged. The other major expansion of activity in this field is a $150 million increase in expenditures for the promotion of public health. The remaining $400 million of the $1.1 billion increase since

1939 is merely the transfer of railroad payroll taxes to a trust fund. These taxes appear on both the receipts and the expenditures sides of the budget, and do not affect the surplus or deficit.

The increase of over $600 million in agricultural expenditures is more than accounted for by expenditures under the wartime program of price supports, enacted to encourage agricultural production by providing a guarantee against an early-postwar price slump. Other financial aids to agriculture declined.

The 750 per cent rise in expenditures for nonagricultural natural resources is due to two developments: an increase from less than $200 million to $800 million in expenditures for reclamation, flood control, and electric power development; and expenditures in 1949 of more than $600 million for the development of atomic energy.

This sharp rise of public works expenditures in the natural resource field is paralleled by that in the field of transportation and communication, though the percentage rise here is not so spectacular, because half a billion dollars was being spent in this field in 1939. A new type of transportation has successfully made its claim for support since 1939; expenditures for airports and other aids to air travel have risen from $17 million in 1939 to $200 million in 1950. But expenditures for the old purposes have swelled too: that for highways by more than $300 million; for navigation aids and facilities, by $150 million; and for the merchant marine itself, by $110 million. In the field of transportation and communication, one item of expenditure other than those for public works has risen sharply. The postal deficit has risen from a few million dollars to more than $500 million.

The greatest remaining rise is in general government. Here the major items of increase are a rise of almost $300 million in the cost of tax collection and public debt management, caused by the great rise in taxes and in the debt, and an increase of $130 million in the government contribution to the civil service retirement system.

Other increases in expenditures from 1939 to 1949 are relatively minor, and mostly within the limits of cost increases.

Why the Increase from 1949 to 1950?

Are not some of these prewar to postwar expenditure trends temporary, and likely to be reversed in the near future? A comparison of 1949 expenditures with those proposed for 1950 will help to answer that question. Perhaps the most important question about the budget is not why it has already leaped so high, but why it is continuing to rise. Why is an increase of $1.7 billions over 1949 recommended for 1950, even excluding the request for military lend-lease which is yet to come?

War-connected expenditures: the defense budget. One fact is at once obvious from the 1949 and 1950 bars on Chart 2: the rise in expenditures is not due predominantly to the new social programs proposed by the President, but to the rise in defense expenditures. Expenditures for defense, as proposed in the President's budget, will rise by more than $2.5 billion; all other expenditures as a group will decline.

In proposing this increase in the defense budget, the President is not accepting the recommendations of the Army, the Navy, and the Air Force. On the contrary, each of the three services, taken separately, feels that a much larger increase in its budget is essential.[1] Each, during the past year, has vigorously campaigned for a much larger amount than that now allocated to it; and, unless restrained by forceful, direct order from the President, each service will no doubt continue to do so.

The defense budget contemplates a military strength in the three services combined to be maintained at the present level of 1,600,000 men on full-time active duty. However, in the present fiscal year only $5 billion, less than half of the year's expenditures, is for pay and maintenance of personnel. The bulk of the remainder is for procurement of munitions — most notably, aircraft; and a fraction of a billion dollars each is being spent for the maintenance and training of civilian reserves, research and development of new weapons, naval ship construction, military construction, and stockpiling of strategic materials.

Expenditure for the pay and maintenance of personnel will rise by $150 million in 1950, even at present rates of pay, and pay increases recommended by the President will bring a further moderate increase. Each of the smaller types of expenditure listed above, with the exception of that for research and development of new weapons, will also rise, the sharpest advance being in stockpiling expenditures. But the bulk of the increase in total defense expenditures will be in procurement, plus a new expenditure of $600 million for the first year of universal military training, if the President's renewed recommendation for such training should be accepted by the Congress.

The rivalry of the three services for funds has been intense. With the present incomplete unification of the services, and the large degree of autonomy granted the Secretaries of the Army, the Navy, and the Air Force, successful coordination of the programs of the three services was not achieved in planning for the 1949 budget, and it was not possible to prevent each service from lobbying for its own program, independently of the other two services, and in fact independently of the program advanced by the President and by the Secretary of National Defense as spokesman for the President.

Recognizing the need for a powerful and up-to-date Air Force, the administration last year recommended a program of Air Force expansion and of aircraft procurement which over a period of several years would increase the strength of the Air Force to 55 combat groups (and 17 squadrons). As the strength of the sentiment in Congress for a much larger program — a sentiment fostered in part by a vigorous campaign by the Air Force itself — became evident, the President later proposed a program of 66 groups. However, even this second proposal was overridden by the Congress, which provided funds for fiscal 1949, together

[1] Contrary to the impression given by Navy statements quoted in recent newspaper reports, both appropriations and actual expenditures scheduled for the Navy in 1950, in the budget proposed by the President, are considerably *higher* than in 1949.

with the authority to make contracts extending over a longer time, sufficient to inaugurate a program leading to an air strength of 70 groups within four years.

Though no official figures of the cost of this program, together with related programs required to make it effective, for 1950 and later years, were released, it was commonly estimated at the time that the resultant total defense budget would be more than $14 billion in 1950, and perhaps $16 billion in 1951, not including the additional cost which would be involved if universal military training and a program of military aid to western Europe were adopted.

In presenting the 1950 budget, the President has again recommended that the size of the Air Force be held below that contemplated by Congress last year. His present recommendation is for "a minimum" of about 48 combat groups and 10 squadrons.[2] He estimates that the cost of a total national defense program incorporating this proposal will be $13.7 billion in 1950, excluding the cost of universal military training, and with it the defense budget for 1950 totals $600 million more, or $14.3 billion. The cost of universal military training, the President adds, would rise to perhaps $2 billion in later years.

The existence of conscription authority has raised enlistments in the armed forces to a level at which the forces are now at full authorized strength. Because of this, it seems doubtful that Congress will follow the President's recommendation that universal military training be enacted. Failure to do so would of course reduce the defense budget by $600 million. However, in view of the strength of Congressional sentiment for a larger Air Force than that recommended by the President, it is possible that Congress may offset the "saving" on universal training by increasing appropriations for the Air Force.

Even if the President's lower program is enacted, excluding universal military training, an increase of perhaps a billion dollars from 1950 to 1951 is to be expected, primarily because of increased expenditures for aircraft procurement as deliveries are made on contracts let previously. If the 70-group Air Force program is again reflected in appropriations this year and next year, the defense budget will probably rise by $1.5 billion from 1950 to 1951.

Declines projected in other war-connected programs. The President's budget indicates a decline of $850 million from 1949 to 1950 in all expenditures other than defense expenditures. However, this decline is concentrated within other *war-connected* expenditures — specifically, in expenditures for international affairs and finance, and for veterans' services and benefits. Expenditures for these two functions decline by $1.8 billion.

The largest decline is that of $1.3 billion in expenditures for veterans' services and benefits. The major factor in this decrease is simply the fact that veterans' rights under the "G.I. Bill"

[2] Under the 1950 budget, aircraft deliveries in fiscal 1950 will be about 37 million pounds. This compares with minimum deliveries of 56 million pounds which the report of the President's Air Policy Committee (the "Finletter Report") recommended for calendar year 1949, in order to sustain the productive capacity of the airplane manufacturing industry.

to educational benefits, and to unemployment and self-employment benefits, are rapidly running out. Expenditures for educational and training benefits will decline from $2.5 billion to $2.0 billion; and those for unemployment and self-employment allowances, from $420 million to $80 million. The only other major factor of decline in expenditures for veterans is that a special governmental payment of $400 million into the veterans' insurance fund in 1949 will not recur. Expenditures for construction of veterans' hospitals and related facilities will increase slightly, whereas current expenses of the Veterans' Administration, both for medical care and for general purposes, will decline somewhat.

The $500 million decline in expenditures for international affairs and finance will occur primarily because of an anticipated decline in the cost of the Army occupation of Germany, as the European Recovery Program improves conditions there, and because of the dwindling away to zero of expenditures still being made in fiscal 1949 to complete payment for programs long since ended under the UNRRA and post-UNRRA programs. The decline in expenditures under present programs of aid to China, Korea, Greece, and Turkey is largely offset by provision for new, unspecified foreign-aid programs which had not yet been fully formulated when the budget was prepared. Current developments in China may of course affect these plans.

Expenditures under the European Recovery Program in 1950 are estimated at $100 million below the 1949 figure of $4.6 billion. A greater decline is expected after 1950.

To these existing international programs will be added, when it is fully formulated, a proposal for lend-lease military aid to the "Western Union." This proposal may well convert the decline of $500 million in international expenditures to an increase.

The remaining type of expenditure which I have classed as war-connected, namely, interest on the public debt, will rise slightly because of higher interest rates.

Non-war-connected expenditures: declines in some programs partly offset increases. The remaining sector of the budget is less directly connected with war and its aftermath. Within this sector, expenditures for agriculture and for transportation and communication decline moderately; several functions embodying the new social program of the President rise by a combined total of $600 million; those for natural resources rise because of the increasing cost of public works projects already authorized; and other programs remain approximately constant.

Because of increasing expenditures, largely under programs already authorized, for highways, for airports and other aids to aviation, for navigation aids and facilities, and for the merchant marine, the public works expenditures included under the function "Transportation and Communication" are rising. Total expenditures under this function decline only because of an estimated decline of $100 million in the postal deficit even with existing postal rates, and the recommendation of increases in postal rates which would reduce the deficit by a further $250 million.

Expenditures for agricultural purposes are expected to decline because of an anticipated reduction in price-support expenditures made under the wartime program of agricultural price supports, which extends through the 1949 crop year. The sharp decline in 1948 in the prices of basic crops resulted in price-support expenditures on a large scale. Crop yields in 1948 were above "normal" because of exceptionally favorable weather. If they decline to normal in 1949, the reduction in production of the basic crops will reduce price-support expenditures. If crop yields are as high as in 1948, expenditures for agricultural purposes will probably not decline.

Public works expenditures are rising, not primarily because of new projects recommended by the President, but because of the increasing cost of projects authorized by the Congress during the past two years. Large projects of reclamation, flood control, and electric power development necessarily pass through a planning stage after authorization, and thereafter gain momentum as construction is started and comes into full swing. Annual costs therefore rise for several years. Mainly for this reason, expenditures for the development of our land and water resources (included under the function "Natural Resources Not Primarily Agricultural"), which jumped from $500 million in 1948 to $800 million in 1949, will rise further to almost one billion dollars in 1950.

The rise would be greater except for the veto by the President of all but the most urgent of a considerable number of strongly supported proposals for additional projects. The few new projects which he has recommended are mainly for public power development in areas where the power supply is very tight. It is entirely possible that Congress will again — as it did last year — authorize projects not requested by the President. Many added projects, taken individually, have plausible economic justification, and would yield considerable economic return to individual regions or communities. The President vetoed a number of these, not because they seemed economically unsound, but because their construction at this time did not seem sufficiently rewarding to justify the resulting inflationary pressure. This situation points up the fact that the present level of public works expenditures is not due to a short-lived postwar spurt in these expenditures. The public attitude toward programs in this field is such that expenditures will be at their present level or a higher one for many years.

The President's new social programs. The remaining change in expenditures between 1949 and 1950 results from the new social programs recommended by the President. It may seem astounding, in view of the range of the programs recommended, and the magnitude of the proposed medical-care insurance program and the proposed changes in old age insurance and unemployment compensation programs, that all the proposals combined result in an increase of only $600 million in expenditures. The explanation is that the increased revenues from payroll taxes to support the three social insurance measures mentioned will not flow into general Federal revenues, but will

be held in trust in special funds; expenditures will be made from these trust funds, and will not form a part of budget expenditures. This, of course, is the way in which present social insurance programs are handled.

These social insurance proposals are so important a part of the President's economic program that they deserve discussion even though they lie outside the budget proper. The President proposes two important changes in existing social insurance programs, and the establishment of two new programs. He would extend old-age and survivors' insurance to almost 25 million gainfully employed persons not now covered; would sharply raise the scale of benefits; and would provide benefits for women at an earlier age. He would also broaden the coverage of unemployment insurance and increase the level of benefits in some states. The less sweeping of the two new major proposals is the addition of a new type of benefit, compensation for both temporary and permanent disability of workers covered by unemployment insurance. Finally, and in its ultimate effects most important, the President recommends the establishment of a comprehensive system of insurance covering the costs of medical care.

Expenditures under these proposals would rise gradually. For the near future, the costs would be financed altogether from payroll taxes, and hence from trust funds. It is contemplated, however, that part of the increased cost in later years will be borne by general revenues.

A number of other less important social proposals in the President's budget message will not be discussed here, for lack of space.

The new social proposals which do affect the 1950 budget importantly are those for expanded aid for public housing; for Federal aid to education; and for an increase in Federal grants for assistance to aged persons who are not now eligible for benefits from the old age insurance funds, to the blind, to dependent children, and to other special groups. Proposed legislation which would broaden this public assistance somewhat would increase expenditures by $65 million. Various state and local agencies have an important, direct interest in these programs.

The major planks in the President's housing program are loans and grants to municipalities for slum clearance and urban redevelopment, and annual contributions to the operating expenses of local public low-rent housing. In addition he recommends loans and certain grants for farm housing, and authorizations for mortgage purchases to stimulate co-operative and private low-rent housing. While expenditures for the two major housing programs would amount to only $139 million in 1950, it is contemplated that they would rise to a combined total of not far from a billion dollars in 1954. The actual rate of increase, if the legislation is enacted, would not be so rapid unless local governments pressed forward slum clearance and public housing plans with great speed.

In one other proposed social program, the President breaks with tradition as sharply as in the housing program. He renews his recommenda-

tion for Federal aid to education, at a level of $290 million in 1950.

Continuing High Budgets and Their Effects

What are the prospects for budget reduction through economy? This summary of the nature of major increases in Federal expenditures suggests the continuation of high budgets for an indefinite period. They are based upon persisting international tension and important domestic programs with widespread support. The forecast of continuing high budgets is unaffected by recurring drives for reorganization and economy in government. Probably the most important single truth which the citizen should know about the budget is that the great increase in expenditures since 1939 is due, not to bureaucratic waste, but partly to cost increases and partly *to a great expansion of the services and financial benefits furnished by the Federal government.* No amount of campaigning against bureaucratic inefficiency, or even of constructive administrative reorganization, will effect any *major* reduction in Federal expenditures. Such a decrease can result only from a significant curtailment of the services or benefits furnished by the government to the country as a whole or to special groups of citizens.

Less than one-sixth of Federal expenditures are for civilian payrolls; and of all Federal civilian employees, more than three-fourths are employed in the National Military Establishment, the Post Office, or the Veterans' Administration. The bulk of total expenditures are for military payrolls, procurement, and related expenditures; for interest on the public debt, management of the $252-billion debt, and tax collection; for the European Recovery Program; for reclamation, flood control and related river-basin development, and highways; for services to veterans; for farm price supports, or for direct financial aids to special deserving or dependent groups such as veterans and the aged. He who would reduce the budget significantly must eliminate or curtail some of the services or benefits being furnished.

Some economies are of course possible through greater efficiency. It is a reasonable guess that the possibilities may be greatest in the National Military Establishment and the Veterans' Administration, since they have grown rapidly to large size, and the process of expanding with great speed to do a large job often involves costs which can be eliminated later. The reports of the Hoover Commission will probably be valuable in suggesting changes which can bring financial economies in these and other agencies — though it should be noted that financial economy in the narrow sense is neither the only nor the main purpose of the Commission. But the maximum economy which might be achieved without loss of services now rendered should probably be thought of as a small percentage of the budget.[3]

The effect of the budget trends on employment and inflation. In conclusion, it is worth while to note briefly what the economic impact of the trend

[3] In the judgment of the writer, the Hoover Commission estimate that $3 billion can be saved is too high, even as a goal which might be achieved under ideal conditions.

in the total budget from calendar year 1948 to calendar year 1949 will be. Budget expenditures will rise sharply from the one year to the other. Expenditures are rising during fiscal 1949; i.e., will be higher in January-June, 1949, than they were in July-December, 1948. For the last half of 1949 they will probably be still higher (after allowance for seasonal swings) because of the increased 1950 budget. Furthermore, payments of various types to the public from the social insurance trust funds, not included in the budget, will also increase. In addition, during fiscal 1950, an accumulated dividend from the National Service Life Insurance fund, now estimated at $2 billion or somewhat more, will be paid. For these various reasons, it is estimated by the President's Council of Economic Advisers that cash payments to the public by the Federal government will rise from $37 billion in calendar 1948 to more than $44 billion in 1949.

On the receipts side, Federal cash receipts from the public (including trust fund receipts) will tend to rise from 1948 to 1949 because of the proposed increase in payroll taxes, and for certain other minor reasons. These increases, however, will be more than offset by the tax reduction effective in mid-1948, so that cash receipts from the public will fall, it is estimated, from more than $45 billion to less than $44 billion.

The combined effect of these changes is that while the Federal government is paying out $7 billion more to the public, thus augmenting total private income and demand, the restraining effect on demand of government tax collections will be lessened.

The President's economic advisers estimate that this increase in demand resulting from the Federal fiscal changes may be too great for safety — that it may induce further inflation. It is avowedly for this reason, rather than solely because a budget deficit of $900 million is forecast for fiscal 1949, that the President has recommended tax increases. The ramifications of these tax proposals lie outside the scope of this article. Whether they should be passed at all has been questioned in view of the recent price declines, though it is by no means clear that the down trend will continue.

Price Level Prospects*

V Lewis Bassie

Director, Bureau of Economic and Business Research

PRICE LEVEL prospects are dependent on the future of general business activity. That is a relationship well established by the economic experience of the last few decades. It is particularly true of farm prices, since farm products go so directly into consumption, and the income of consumers is so directly dependent upon employment in industry and trade.

When business is good, prices are never too low; when business is bad, prices can be maintained only by certain strong monopolistic groups, and farm prices typically bear the brunt of the decline. Before dealing with future price levels, therefore, it is necessary to consider the general business outlook, analyzing the strategic economic factors that will determine business conditions in the months ahead.

Fears That Affect Business

Just now, fear seems to have the upper hand — though many who fear a general decline feel that their own business position is sound. One of the most important current sources of fear is the existing tension on the international front. We cannot afford to minimize the dangers which exist in the present struggle for control of Europe and Asia, but the situation does bring to mind the thesis of a historian I know that after every war the victor takes measures to protect himself against the possibility of future attack. Today, we are victors; and we are making just such preparations. What makes the tension so acute is that we have only one opponent worthy of fear; and that opponent is also a victor, also fear-ridden, and also undertaking the same kind of protective measures we ourselves feel to be necessary for our safety.

The uncertainty generated by this international situation seems to carry over into our day-to-day affairs. It is as if we are continually interrupting our work to glance over our shoulders to make sure the Indians aren't dashing out of the woods before we can get our stockade completed. There is little we can now do about this situation. As time passes, however, we shall view it in truer perspective, and more calmly.

The other basic fear is fear of a recession in business, with all its attendant evils of unemployment, reduced incomes, and business failures. We carry over in our minds memories of the dark days of depression and possibly that is one reason why inflation does not impress us as the real economic bogey man.

In recent months the fears of a decline have been whipped up to an extreme pitch of excitement by the so-called "experts" and commentators who are able to gain more attention by crying wolf than by any impartial presentation of facts. With the economy in an apparent state of balance that lends support to views on both sides, and

* Address before the Farm and Home Week Program, University of Illinois, February 1, 1949.

heightens feelings of uncertainty, it is easy to play up and exaggerate almost any sign of weakness. Thus temporary and partly seasonal declines in consumption take on the character of a "buyers' strike." Similarly, declines in farm prices resulting from record crop production and good crop prospects are magnified by efforts to reduce inventories and proclaimed to be omens that interpret the handwriting on the wall.

There is little appreciation of how much the so-called "present recession" is due to the weather. It was the perfect weather sequence that brought us the record crops last year. It was the mild fall that held back sales last November. And now the winter storms have again contributed to declines in sales and production. Few people recognize the weather as a temporary factor that usually averages out over a period of time.

Strong Elements in the Economic Outlook

In contrast to the current wave of fear and farm price deflation, there are at least two reasons for expecting business prosperity to continue for another year or so. These are the rising trend of government expenditures and the construction boom. As long as these important elements continue so strong there can hardly be an appreciable letdown.

In the fiscal year 1948 — that is, the year ended last June 30 — Federal expenditures were at a postwar low of $34 billion. Expenditures in fiscal 1949 are estimated at $40 billion. And the budget recently put before Congress by President Truman calls for expenditures of almost $42 billion in fiscal 1950.

There is a distinct probability that actual expenditures in the coming fiscal year will exceed the budget estimate. This is true of military expenditures, for example. Increases for the next two or three years were programmed in Congress last year and are as likely to be increased as cut back by the present Congress. Even if the budget is passed as it stands, total authorizations to the military agencies will exceed the budget expenditures estimate by over a billion and a half. To the extent that these agencies are able to push their programs along more rapidly, military expenditures may be increased over the estimate.

In addition, the budget estimates do not include military aid to Western European countries; this program is to be given separate consideration later.

They do include the continuation of the present foreign aid program at a high level. The Economic Cooperation Administration program is just moving into high gear. About 90 per cent of its current funds are now allocated; and with purchase approvals moving up even faster than allocations, a rising trend in procurement and shipments can be expected. The peak may be reached next summer, and the proposed new appropriation is large enough to ensure that the subsequent decline will be slow.

How far these military and foreign aid programs may be pushed depends on the course of international affairs. No one can tell just what the turn of events will be, but it seems likely that we shall have a prolonged period of

cold-war tension without open hostilities.

Another important payments item — one not considered a budget expenditure — will be the refunds to veterans of excess insurance payments, to be made in the latter half of this year. These are variously estimated at anywhere from $1 to $3 billion.

State and local government expenditures have also been rising sharply. They have passed the $18 billion level and are now running a half-billion higher than receipts. Because of the urgent needs for many of the programs covered by these expenditures, both the expenditure total and the deficit to be covered by borrowing will continue to increase in the period ahead. As an example of the backlog of demand in this field, I would like to cite the recent report that Illinois alone needs $2½ billion of work to fix up its roads. That report said nothing about schools, hospitals, community facilities and other needed building. Generalize this situation for all 48 states, and you come up with an astronomical total that has barely been touched by construction work already completed.

According to the report of the Council of Economic Advisers, total cash payments by all government units will "rise to perhaps $61 billion for the calendar year 1949, more than $9 billion higher than in 1948."

The increases in these programs should be more than enough to compensate any foreseeable declines in other important segments of the economy. In fact, the magnitude of the increases is so large as to suggest that the present downswing in prices may again be reversed, as it has in each of the last two years. For the domestic economy still seems strong enough to make a pretty good case for itself. Construction gives every indication of continuing at high levels. The joint estimates of the Departments of Commerce and Labor place total private construction for 1949 slightly higher than in 1948. In this total estimate, slight declines in residential, farm, and industrial construction are more than offset by increases in commercial and public utility construction. With costs now practically stabilized, and estimated to continue so, this means a sustained level of construction activity throughout the year.

The key to higher or lower expenditures in this field lies in privately financed housing. Last fall, residential construction was lagging somewhat behind the level in the corresponding months of 1947. In December, however, the number of units started was again close to the number started in December, 1947. The difficulty of making a precise forecast arises from the shifting of seasonal patterns. It is clear that builders are no longer under pressure to put up so many units in the cold season. How much this shift may affect the total for a whole year will not be definitely known until after the seasonal upswing is under way next spring.

The retarding elements in the housing picture are of course high construction costs and the tightening of the mortgage market. These, however, do not seem to be insurmountable obstacles. While the demand for housing is unquestionably restricted by costs it

is nevertheless large enough to sustain the boom through 1949. As for financing, there is little to encourage any idea that funds are lacking. The only question is one of terms and rates; and even after recent increases interest charges are a smaller portion of the total costs of home ownership than in past periods of high construction activity. All in all, there is a definite possibility of at least reaching the 1948 level of housing expenditures; and the official government estimates for 1949 can be regarded as slightly on the conservative side.

For the longer run, the significant point about these high costs and tighter mortgage terms is that they will have more of an effect in cutting the top off the boom than in bringing it to a quick end. If the boom should continue with a flattened top, and with costs stable or tending downward over a period of time, rising incomes will tend to recreate the market that has been temporarily wiped out by high costs and mortgage restrictions. Then, though the boom does not get quite as high as it might in any one year it may well last longer.

Weaker Elements Are Not Decisive

Business investment, other than construction, has been showing some signs of slacking off a little and over the longer run can no longer be regarded as a force on the upside. Expansion goals of many businesses have been met, and new equipment expenditures by these firms will be lower in the future. However, others are still expanding; and in all lines of business, the need for modernization to increase efficiency or to improve products is keeping new machinery and equipment installations high.

Total expenditures for machinery and equipment now constitute a larger share of the national output than in prewar prosperity periods. At the peak annual rate of $21 billion reached in the last half of 1948 they may thus be considered a little in excess of normal. Although it seems reasonable to believe that any excess over normal will be eliminated in the coming year, this moderate cutback would not be sufficient to initiate a recession. In fact, the timing of the decline corresponds almost exactly with the switch of ECA programs from relief to capital goods. Any release of capacity in the machinery industry will permit filling the orders of foreign purchasers who need equipment to complete their reconstruction and development programs.

Another factor sometimes considered likely to bring on a decline is the swing of business inventories. Commerce Department figures showed manufacturing and trade industries to have reached a record high of $54 billion. The postwar increase in dollar value has unquestionably been large; but the advances that brought inventories up to this high level were in large measure advances in the prices of existing goods and not new accumulations. Inventories are now more nearly in line with sales than in the war period but the inventory-sales ratio for October was still twenty percent lower than prewar; and there is little evidence that inventories are overburdening. In the few lines where they are reported to be heavy, such as men's clothing, businessmen at all stages — manufacturers,

wholesalers, and retailers — have been taking drastic action to bring them down.

Signs of inventory liquidation in the last few months have been apparent on every hand. Worried businessmen have given their fears tangible economic form in cutbacks designed to reduce inventory risks. At the end of 1948, department store orders outstanding were little more than half the volume of a year earlier. The layoffs that swell the ranks of the unemployed reflect the same reaction at the manufacturing stage.

But inventory policy is as variable as the weather, and as equally subject to quick reversal. Liquidation cannot long continue in a period of sustained activity. And if a definite reversal should again take place, inventory accumulation could play an important part in a new inflationary upsurge.

Summing up at this point, it seems likely that the total of all these strategic types of expenditures will be higher a year hence than it is now. This is important not only in itself but for its implication that consumer incomes and expenditures will advance correspondingly. It indicates that the gross national product will be running at least several percent higher at the end of 1949 — say, at an annual rate $10 billion higher than in the fourth quarter of 1948.

Consumers' Expenditures Continue High

Preliminary estimates indicate that consumers' incomes and expenditures were well maintained through 1948. Immediately following the end of the war, production of many types of civilian goods was renewed or expanded, consumer expenditures rose sharply, and savings were drastically reduced from the high wartime rates. In the second quarter of 1947, savings were at an annual rate of only $4 billion, or two and one-half percent of income after taxes. The lagging of expenditures since that time has restored savings to a more normal level. In the last two quarters of 1948, consumer expenditures and savings were again moving in line with income.

Two explanations of the lagging of expenditures in the last year and a half have received prominent mention. These are buyers' strikes and the squeeze on low-income groups. On closer analysis both of these explanations appear to be fallacious. As for the first, there is no good evidence that a buyers' strike was ever effective in this country. It is true that just before the collapse of 1920, which is sometimes referred to as a buyers' strike, consumption was restricted; but consumers had little choice in the matter. Their consumption was simply squeezed as the speculative drive for inventories pushed prices up; and the available data do not indicate that consumer resistance was otherwise important in bringing on the decline.

As for the second, analysis of the income distribution and of liquid asset holdings of families and other consuming units does not indicate that any large part of the population is so much worse off that aggregate expenditures might now be lowered. The income distribution is in fact more favorable to high level consumption than in prewar

years. Furthermore, although the lowest income group has been drawing upon savings to finance its expenditures to a greater degree than before the war, the holdings of liquid assets in that group rose during the last two years. Accumulated savings are still well distributed through all income groups.

There is little need to look for explanations, either favorable or unfavorable, of the postwar changes in consumption and savings. The fact is that consumers were temporarily spending more than the normal proportion of their incomes, and now they have let their expenditures drop back. It is a development that should have been expected. It cannot be considered a continuing force for deflation.

In the last few months, since the decline in prices began, the flow of goods to consumers has definitely accelerated. This points to one of the most favorable aspects of the situation — namely, that further price declines, or further increases in incomes with prices stable, will tend to increase consumption. In other words, there is a large potential demand for various kinds of goods as soon as price declines bring them within the budgets of consumers who have been squeezed by the high cost of living. A moderately declining price level by no means holds the prospect of reduced production and employment.

Neither Inflation Nor Deflation

Turning now to the question of prices, it cannot be said that a serious decline is anywhere in sight. Demands of government, business, and consumers all give promise of continuing high; and until aggregate demand falls off there will be no serious break in the general price level. From a short-run point of view, there is some likelihood that the price advance will be temporarily renewed in the latter part of the year.

From a somewhat longer-run point of view, it seems that the inflation has largely run its course. The factors underlying the recent declines may be summed up under two headings — increased production and reduced backlogs of demand. Even in the industries where backlogs of demand were greatest, and limitations on production were most severe, there has been a return to a more normal situation. This is true of some non-durable goods, like petroleum and chemical products, as well as most types of consumer durable goods, like radios and most of the electric appliances. Even in the automobile industry, delivery dates have been shortened, and higher-priced cars may be obtained on immediate delivery. In particular lines, of which these are only examples, adjustments have been taking place from time to time all through the last two years. These adjustments are a sign of progress in the fight against inflation and will continue as bottlenecks are broken and key production problems are solved. We can depend on the tremendous productivity of this country to prevent prices from again going much higher.

On the other hand, a sound case cannot be made for general deflation in the near future. The recent declines have centered on prices of farm products and foods. The combination of record production and unwillingness to hold available supplies is the basis of these de-

clines. When the harvest is in, and everybody wants someone else to assume the risks, there is no telling how far a decline can go. In particular, when the large processing industries refuse to maintain inventories, there may be no comparable source of buying power in the market. Presumably, the speculative markets are then "forced" to take over. But these markets can be "forced" only at a price; and if the speculators also are fear-ridden, the bottom drops out.

It is the effects of precisely such a collapse that the government price support program is designed to correct. Under it, the farm community can never be so seriously depressed as to affect the whole economy. Today, government holdings of wheat amount to more than the total carryover expected this year, and the trade will have to draw on these holdings before the new harvest.

Forecasts that 1949 crops will again be overwhelming are without firm foundation, though they seem to have given prices another downward shove. This picture can, of course, change very quickly, as it did in the fall of 1947, and again in the summer of 1948. At the same time, large export markets will persist for a while; and the government's role may yet prove to be just that of maintaining the ever-normal granary, balancing out temporary differences in the levels of demand and supply. It is much too early to predict that the government will incur a sizable loss on its purchases either this year or next. If it does, the program will be reshaped, but not in the direction of abandoning price supports.

Analogies Do Not Hold

Why, then, have the fears of a collapse been so persistent? In part, they are based on the idea that what goes up must come down. This is one of those simple propositions that seem attractive at first glance but have little real merit. There is no immutable law of gravitation in economics. A boom does not end just because a boom cannot go on forever. It ends because there is a decline in the expenditures that were forcing prices up.

This simple theory can readily be backed by analogies from past history. In every war, the price level has made tremendous advances; and after every war it has again fallen back. It is regrettable that we lack information to bring out the differences in all these postwar situations. Yet, there can be no question that there have been differences. Has war ever before been followed by the present kind of "cold war"? Were the incomes of the whole population ever before inflated during a war period to a degree corresponding to the general level of prices?

Today, real disposable income per capita, that is, the income at our consumers' disposal after payment of taxes and after allowing for higher prices and for the increase in our population, is more than a fifth above the prewar record of 1941 and more than a third above the prosperity peak of 1929.

In part, also, the argument of the pessimists is bolstered by a kind of circular reasoning. The price weakness is taken as an indication of more general economic weakness. The price reversal, it is felt, will bring on liquidation with consequent declines in production and

employment. Only rarely, however, in those speculative situations where stocks are piled up and then quickly thrown back on the market, are the price changes controlling. That was the kind of boom and bust following World War I.

The situation today is quite different from that of 1920. This boom is not primarily based on speculation. There has been no inordinate piling-up of inventories, no pyramiding of insecure loans and credit. We have already been through the transition period needed to get the construction industry into full swing and to bring output up to a high level in the reconverted durable goods industries. We have private investment and government expenditures running at the rate needed to maintain current income flows, and we have the structure of incomes inflated to correspond with the level of prices. With these facts in mind, it can be firmly stated that the mere fact that prices are high does not mean that they are about to come down.

We may now hope for a period of prosperity, with national income generally rising, and the level of prices tending downward as more and more prices are brought back into line. This does not mean that all our economic problems have been solved. We cannot see much farther than a year ahead, and even that depends on our international affairs. But as far as we can see, the outlook is bright.

Books Reviewed

The Business of Farming. By Herrell DeGraff and Ladd Haystead (Norman: University of Oklahoma Press, 1948, pp. xviii, 244. $3.00)

Not often does one have the opportunity to read a book so comprehensive and yet so simply written as *The Business of Farming.* The authors introduce the reader to all the basic and most important problems connected with farming and farm management, pointing out methods of solving some of them. All this is done in such an interesting, easy-to-read way that I agree with True D. Morse, who wrote the foreword, when he says, "This is a delightful book."

The theme throughout the twenty-seven chapters is that management of the inputs of land, labor, and capital can make or break the farm, and that, in this day and age, *good* management is a necessity if farming is to be a successful profit-making business over a period of years. Absentee landowners and businessmen from the city who are considering investment in farm land can well afford to read this book. In fact, they *should* read it.

The material is organized into four parts. The first three have to do with management of the soil, equipment, and labor, and the fourth with the more inclusive problem of fitting these other factors of production into a profitable, balanced farm unit.

One quality of the book is its breadth of viewpoint. The authors have not attempted to force "one man's opinion" down the reader's unwilling throat. Instead, they have summarized high spots in the thinking of many noted agricultural authors from various parts of the United States. The farms and the types of farming used as examples throughout the book range from the "ten acres and a mule" sharecropper farm of the South to the Seabrook Farms of New Jersey, the world's largest vegetable farm and processing plant. The kinds of farmers discussed (and criticized pro and con), are as varied as the farms, reaching from the Louis Bromfield type of grassland soil conservationist, on the one hand, to the "soil miner," the man who takes all and puts nothing back, on the other.

The ideas in this book are not new. They are merely presented in a modern, more digestible way than in many other books on farm management. The reader is not bored with complicated-sounding economic rules and pages of statistics. Yet, indirectly, the principles are all included in the discussion, and enough tabular data are presented to establish important points. At the end of the second part, which deals with equipment management, the authors make the following statement: "Some persons might disagree with the conclusions drawn and logically demand more statistics of similar accomplishments. But in many ways a farm business refuses to be a statistic. Hardly any two farms are alike, and hardly any two farmers are alike. . . ."

Nor is this a static book. It stresses the point that successful management must, of necessity, be dynamic. A good manager never assumes that he has found the all-time answer to his farm organization. Instead, he continually looks for new methods, new varieties,

new ways of increasing efficiency and cutting costs. Therefore, the authors do not attempt to draw hard-and-fast conclusions, but merely point out methods by which a good manager will study his business and work out his own answers.

Most books on farm management are written as textbooks. This one is not — although it might well be used for elementary courses in that subject. It is well adapted for reading and digestion by tenants and landlords, owner-operators and absentee landowners, farm managers, and city businessmen interested in farms and farming.

It should be of great value to anyone who is contemplating buying a farm, especially to those unfamiliar with farming who expect to find a "rustic simplicity in living" and who want to spend their "lazy hours under a vine-shaded porch, . . . with rich rewards of country smells, country tastes, and country feelings." It should be a good reminder to all farmers, farm managers, tenants, and absentee landowners of the problems with which they must cope if they are to realize over a period of time the greatest net money reward for their investments of land, labor, capital and management.

The quotations given with the titles at the beginning of each of the four major parts pretty well summarize the feelings expressed by the authors throughout the book.

"Success or failure in farming starts with the soil."

"Tools can keep you in the black or dump you in the red."

"Your labor is worth what it produces."

"The real problem is management. Land, equipment, labor, livestock, and production supplies are just crazy quilt pieces until put together in a well-balanced pattern."

W. N. Stevenson

College of Agriculture

Managerial Control of Business. By George T. Trundle, Jr., and Associates (New York: John Wiley & Sons, Inc., 1948, pp. viii, 403. $5.00)

The book is well planned for executives of large manufacturing firms. The contents of the entire 403 page volume are summarized in the introduction, which furnishes a very useful check list for mapping out an orderly search for lost or disappearing profits.

The discussion of management problems, though presented in a workmanlike manner, is treated with the bias of the accountant or methods man. The chapters on organization give a precise picture of the general operating relationships and functions which managers must take into account in reviewing or setting up an organization.

The material on budgetary control is excellent and comprehensive. The presentation of the graphical method of expense analysis and the cash forecasting method is forthright and down to earth. However, the discussion of other control problems becomes very technical, and the accountancy vocabulary comes too far to the fore. The section on executive reports is excellent and the step-by-step analysis shows how valuable an executive report can be.

The section on compensation opens on the shaky platform that the source of practically every personnel problem is pay, a very dubious presumption. The

authors go on to summarize the payment methods currently used in industry, and present a clear analysis of salary, incentive, and profit-sharing plans.

The market survey coverage, although formidable, gives a comprehensive overview of the available techniques. The material on sales methods is principally descriptive and furnishes a valuable summary for sorting out those methods that might apply to a particular business situation. Here again the strong bias toward the industrial field excludes any consideration of sales methods or problems in the field of retailing, a bias which dominates the entire section of the book concerned with merchandising or sales.

The real substance of the book is the long central section on manufacturing controls. The treatment of production control, methods, layout, plant management, preventive maintenance, production control, and inventory control is outstanding. Most of the newer techniques are discussed and implemented with excellent examples and illustrations. The section on the compensation of labor evaluates and summarizes most of the acceptable plans and presents each alternative with sufficient pros and cons to enable even the layman to make a fairly reliable judgment.

An impressive feature of the book is the clear statement of the duties, responsibilities, and relationships of quality control and production control. The authors, from their wide background in industrial engineering, are certainly well qualified to make this presentation of a subject which has needed clarification.

The last section, on industrial relations, covers the field very briefly, but perhaps with sufficient emphasis to indicate exploratory possibilities for the average industrial executive. The accountancy bias rears its head once more in the section on job evaluation. The standard point plan for evaluation jobs, together with the least squares method of adjusting job points to dollars in wages, is described as an "exact" system. Presented with its numerous statistical supports, it makes an impressive display. After presenting the entire plan, the authors admit its weaknesses by pointing out that wages, in the last analysis, must still be determined by bargaining.

An over-all evaluation of this book would place it in the top bracket as an exposition of methods of control. From the reviewer's standpoint, however, it emphasizes control to the point where it becomes an end in itself — not a means to an end. "Controls" and "management" are not synonymous.

R. Loken

Supervision in Business and Industry. By Robert D. Loken and Earl P. Strong (New York: Funk and Wagnalls Company, in association with *Modern Industry*, 1949, pp. ix, 219. ($3.50)

This small volume contains a tremendous amount of wisdom for the line supervisor. It sets forth for him principles so fundamental as to be useful in any store, office, or factory. It states them so forcefully that top management and foreman alike will be tempted to agree that "there is no job in the

American industrial-commercial structure of more importance."

The attitude of optimism which is evident throughout the book smacks slightly of the super-salesman philosophy — an impression heightened by numerous drawings, greatly oversimplified and full of forced humor. Loken and Strong justify their faith in their plan, however, by pointing out that

> the methods, ideas, principles, and suggestions . . . were developed through supervisor-training conferences held throughout the United States during the last ten years. More than 50,000 supervisors from all types of occupational groups in business, industry, government agencies, and the Armed Forces participated, adding their ideas to those of the conference leaders.

Successful supervision is said to be possible only if certain basic principles are observed: unity of command, which gives a person only one boss; span of control, which limits the number of subordinates to a maximum of seven; homogeneous assignment, whereby a worker has duties of a related nature; and delegation of responsibility, with requisite authority.

Specifically exempting the creation of job skills from the scope of their discussion, the authors tell how a supervisor can be effective in managing jobs and men. For the first, he must organize, plan, and control the work. Allocating this responsibility to the line supervisor is a practice which has been followed increasingly and with excellent results during the last decade but continues to be resisted by many groups in top management. Steps in organizing will include such a definite sequence as the following: analyzing the jobs and positions, setting the jobs into some structure to show their operating relationships, and carefully selecting men for the jobs. Planning on these lines is regarded as setting up "the schedule for the conversion of ideas into action." It allows the workers a part in the development of plans, but requires that the supervisor make the decisions. With him also rests control, for he is the person in the best position to check up on operations in his department.

The second half of the book is concerned with "Man Management." Whether he is inducting the new employee or increasing the efficiency of a person already on the job, the supervisor's real function is that of teaching. There is a check sheet of thought-provoking questions by which the foreman can evaluate his own skill in instructing the new members of his work force.

In discussing "Problems of People at Work" (Ch. X), Loken and Strong analyze in some detail three types of situations which they regard as typical of the field of human relations problems in supervision. In all three the foreman remains essentially a teacher, whether he is correcting mistakes, handling a grievance, or giving orders.

The reader becomes increasingly aware that the authors are well fitted to give instructions in the method of teaching, for their own pedagogy is sound. Nowhere is this skill more evident than in the chapter dealing with Job Analysis. It should be read by anyone who is responsible for teaching others to perform a job, or wants to teach himself to do his own more ably.

HARRIET D. HUDSON